TRANSCRIPT OF RECORD

Supreme Court of the United States

OCTOBER TERM, 1965

No. 950 63

BANK OF MARIN, PETITIONER,

vs.

JOHN M. ENGLAND, TRUSTEE
IN BANKRUPTCY.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

PETITION FOR CERTIORARI FILED JANUARY 26, 1966
CERTIORARI GRANTED FEBRUARY 21, 1966

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INDEX

RECORD PRESS, PRINTERS, NEW YORK, N. Y., MAY 24, 1966

[fol. 1]

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF CALIFORNIA
SOUTHERN DIVISION

No. 74820

In Bankruptcy

In the Matter of

MARIN SEAFOODS, INC., Bankrupt.

APPLICATION FOR TURNOVER ORDERS—
Filed November 27, 1963

To the Honorable Lynn J. Gillard, Referee in Bankruptcy, at San Francisco, California:

The application of John M. England, respectfully represents:

1. That the bankrupt above-named filed its voluntary petition in bankruptcy on September 26, 1963, and was thereupon, and on said date, duly adjudged to be bankrupt within the meaning of the Bankruptcy Act.

2. That your applicant was, by this Court, duly appointed as Receiver of said Bankruptcy estate, on September 30, 1963, was qualified as such, and did act as such until October 30, 1963, at which time your applicant became, and now is, the duly elected, appointed, and qualified and acting Trustee in bankruptcy of said bankrupt estate.

[fol. 2] 3. That on the date of the filing of the petition in bankruptcy herein, to-wit: on the 26th day of September, 1963, there was due and owing from customers of said

bankrupt monies for merchandise previously delivered by the bankrupt to said customers, sums in excess of $3,200.00.

4. That without the knowledge or consent of your applicant, the aforesaid bankrupt, through its principal officer, collected certain of the said accounts receivable (or portions thereof) and deposited said collections to the bank account of the bankrupt herein at the Bank of Marin, San Rafael, California, in a commercial bank account therein entitled "Marin Seafoods, Inc.", No. 16-00139, on the dates and in the amounts specified below, to-wit:

Deposits	*Date*
$604.30	Sept. 27
251.51	Sept. 27
503.72	Sept. 27
892.04	Sept. 30
588.45	Oct. 2
207.35	Oct. 3
66.80	Oct. 4
67.92	Oct. 8
TOTAL: $3,182.09	

5. That your applicant on the 2nd day of October, 1962, in his capacity as Receiver herein, made written demand upon said Bank of Marin for all monies due and owing from said bank to said bankrupt; that notwithstanding the fact that deposits to said bank account had been made by said bankrupt as indicated above, said Bank of Marin paid no portion of the aforesaid sums to your applicant herein other than the sum of $168.80.

6. That without the knowledge or consent of your applicant, said Bank of Marin did pay over unto Eureka Fisheries, dba Eureka Seafoods, on or about October 2, 1963, sums totalling $2,355.07 of the amount so deposited to the Bankrupt's aforesaid bank account.

[fol. 3] Wherefore, your applicant prays that the said Bank of Marin be directed forthwith to pay over unto your applicant herein the sum of $3,013.29; or, alternatively, that Eureka Fisheries, dba Eureka Seafoods, be directed to turn over to your applicant herein the sum of $2,355.07, and that Bank of Marin be directed to turn over to your applicant herein the sum of $658.22, or for such other, different orders and/or relief as may be meet and proper in the premises.

John M. England, Receiver.

Dinkelspiel & Dinkelspiel, By: Harold A. Block.

[File endorsement omitted]

[fol. 4]

IN THE UNITED STATES DISTRICT COURT

FOR THE NORTHERN DISTRICT OF CALIFORNIA

SOUTHERN DIVISION

No. 74820

In Bankruptcy

[Title omitted]

ORDER TO SHOW CAUSE—Filed November 27, 1963

At San Francisco, in said district, on the 27th day of November, 1963:

Upon the annexed application of John M. England, Trustee herein, praying for certain turnover orders, and/or other relief against Bank of Marin, and/or Eureka Fisheries, dba Eureka Seafoods, good cause appearing therefor, and no adverse interest being represented; it is

Ordered that Bank of Marin and Eureka Fisheries, dba Eureka Seafoods, each show cause before me, in Room 144, Post Office Building, Seventh and Mission Streets, San

Francisco, California, on the 20th day of December, 1963, at 10:00 o'clock a.m., of that day, or as soon thereafter as counsel can be heard, why they, and each of them, should not forthwith pay over unto the Trustee herein, a [fol. 5] total sum of money amounting to the sum of $3,013.29, and why this Court should not grant said applicant such other and further relief as is just; and it is further

Ordered that not later than five (5) days before the date set for a hearing of this Order to Show Cause there be filed herein by said respondents, and each of them, their respective answers to said application, and that they, and each of them, serve copies of said answers within said period of time, as above stated, on Messrs. Dinkelspiel & Dinkelspiel, the attorneys for the Trustee herein, at their offices, to-wit: Suite 1220, 405 Montgomery Street, San Francisco, California; and it is further

Ordered that service of copy of this Order and of the application upon which it is made by a person over eighteen (18) years of age, not a party to this proceeding, by delivering the same to Bank of Marin and Eureka Fisheries, dba Eureka Seafoods, on or before the 10th day of December, 1963, shall be deemed good and sufficient service thereof.

Dated: this 27 day of November, 1963.

Lynn Gillard, Referee in Bankruptcy

[File endorsement omitted]

[fol. 6]

IN THE UNITED STATES DISTRICT COURT

FOR THE NORTHERN DISTRICT OF CALIFORNIA

SOUTHERN DIVISION

No. 74820

In Bankruptcy

[Title omitted]

ANSWER OF RESPONDENT BANK OF MARIN—
Filed December 16, 1963

Comes now the Bank of Marin and files its Answer to the Order to Show Cause of November 27, 1963;

That the first notice of the Bankruptcy was received by the Bank of Marin on October 3, 1963, at which time no money was in the account of Marin Seafoods, Inc., and in fact, it was overdrawn in the sum of $13.55. (See Exhibits "A" and "B".)

That on October 3, 1963 the Bank of Marin so notified the Trustee, John M. England. (See Exhibit "C".)

That thereafter Marin Seafoods, Inc. deposited $207.35, $66.80, $67.92, deducted $6.00 on October 7, 1963 for service charge on three returned checks, and on October 8, 1963 made a service charge of $4.47, and on October 10, 1963 honored a check to Hugh Bourne for $149.25 and on October 17, 1963, after a letter of October 14, 1963 from John M. England, sent him $168.80. (Exhibit "D".)

That the Trustee's letter of October 2, 1963 did not request any later deposited sums; that the Bank of Marin be-
[fol. 7] lieved that later deposited funds should be honored

if checks were drawn against the account; no Order concerning after received funds was sent to the Bank of Marin; upon receipt of the letter of October 14, 1963, it sent the total balance to the Trustee.

Dated: December 14, 1963.

Bank of Marin, By Burton R. Kirchner, Vice President.

[File endorsement omitted]

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Marin Seafoods, Inc.
19 Lovell Avneue
San Rafael, California

16-00139

DUPLICATE
STATEMENT OF ACCOUNT WITH

BANK OF MARIN

SAN RAFAEL, CALIFORNIA

OLD BALANCE	CHECKS—LISTED IN ORDER OF PAYMENT—READ ACROSS			DEPOSITS	DATE	CHECK COUNT	NEW BALANCE
71.38	4.00	122.19	41.00				
	31.40			278.10	6 Sept	3 4	150.89 S
	119.77				6 Sept	3 1	31.12 S
	112.32	16.50	27.39				
	394.59	368.25		511.93			
				464.49	6 Sept	4 6	88.49 S
	4.00	534.01		523.54	6 Sept	5 8	74.02 S
	289.25	225.60	52.92	506.88	6 Sept	6 11	13.73 S
	140.00	50.50	119.77	569.10			
	10.50	50.00	748.07	854.15	6 Sept	10 17	318.14 S
	55.20	219.22	118.45	181.69	6 Sept	11 20	106.96 S
	527.45	310.65	20.69				
	42.24	40.33		76.61	6 Sept	12 25	757.79 OD
	2.00	2.00	42.30	614.57			
	168.50	55.20	25.10	242.28			
				605.17	6 Sept	13 31	409.13 S
				354.71	6 Sept	16 31	763.84 S
	4.47 SC				6 Sept	17 31	759.37 S
	119.77	180.80	218.00				
	519.00				6 Sept	17 35	278.20 OD
	107.98	2.00	44.87	798.59	6 Sept	18 38	365.54 S
	287.84	397.78		462.32			
				95.14	6 Sept	19 40	237.38 S
	265.61				6 Sept	20 41	28.23 OD
	10.00	55.20	60.23		6 Sept	23 44	173.66 OD
	2.00	55.20	384.21	578.77			
				1,024.75			
				229.26	6 Sept	24 47	1,217.71 S
				375.93	6 Sept	25 47	1,593.64 S
1,593.64	390.50	566.40	6.00				
	569.80	550.00		318.98	6 Sept	26 52	176.06 OD
170.08-	107.98	2.00	2.00		6 Sept	27 55	282.06 OD
282.06-	126.70			604.30	6 Sept	27 60	195.54 *
195.54				251.51			
				503.72			
				892.04	6 Sept	30 60	1,842.81 *
1,842.81	75.24	16.50			6 Sept	30 62	1,753.07 *

DEBIT MARKED SC
REPRESENT SERVICE CHARGE FOR **PRECEDING** MONTH

THE LAST AMOUNT IN THIS COLUMN IS YOUR BALANCE

FORM 88

PLEASE EXAMINE STATEMENT AND CANCELLED VOUCHERS PROMPTLY. REPORT ANY ERRORS OR OMISSIONS WITHIN TEN DAYS OTHERWISE THE ACCOUNT WILL BE CONSIDERED CORRECT.
FOR YOUR CONVENIENCE A RECONCILEMENT FORM IS ON REVERSE SIDE.

[fol. 8]

EXHIBIT "A" TO ANSWER

DUPLICATE

MARIN SEAFOODS INC.
19 LOVELL AVE.
SAN RAFAEL, CALIF. 16-00139

STATEMENT OF ACCOUNT WITH

BANK OF MARIN

SAN RAFAEL, CALIFORNIA

OLD BALANCE	CHECKS—LISTED IN ORDER OF PAYMENT—READ ACROSS			DEPOSITS	DATE	CHECK COUNT		NEW BALANCE
1753.07	609.45	141.68	438.31					
	630.42	492.96	42.25	588.45	630CT	2	6	13.55
13.55-				207.35	630CT	3	6	193.80
193.80				66.80	630CT	4	6	260.60
260.60	6.00				630CT	7	7	254.60
254.60	4.47 SC				630CT	8	7	250.13
250.13				67.92	630CT	8	7	318.05
318.05	149.25				630CT	10	8	168.80
168.80	168.80				630CT	17	9	.00

[fol. 9]

DEBIT MARKED SC
REPRESENT SERVICE CHARGE FOR **PRECEDING** MONTH

THE LAST AMOUNT IN THIS COLUMN IS YOUR BALANCE

FORM 25

PLEASE EXAMINE STATEMENT AND CANCELLED VOUCHERS PROMPTLY. REPORT ANY ERRORS OR OMISSIONS WITHIN TEN DAYS OTHERWISE THE ACCOUNT WILL BE CONSIDERED CORRECT.
FOR YOUR CONVENIENCE A RECONCILEMENT FORM IS ON REVERSE SIDE.

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[fol. 10]

EXHIBIT "B" TO ANSWER

REFERENCES
WELLS FARGO BANK
BANK OF AMERICA
CROCKER-ANGLO NATIONAL BANK
PACIFIC NATIONAL BANK
BANK OF CALIFORNIA

SPECIALIZING AS
CREDITORS REPRESENTATIVE
RECEIVER AND TRUSTEE IN
U. S. BANKRUPTCY COURT

JOHN O. ENGLAND
JOHN M. ENGLAND
155 Montgomery Street
Room 601
San Francisco 4, Calif.

Phone GArfield 1-4327

October 2, 1963

Bank of Marin
836—4th Street
San Rafael, California

Re: MARIN SEAFOODS, INC.

Dear Sir:

Please be advised I am the Receiver in the above entitled matter. The schedules of the bankrupt and statements received from your bank indicate certain money on deposit with you.

I am enclosing herewith a certified copy of the order approving my bond and ask that you forward a check for the balance on deposit in the name of said bankrupt.

Very truly yours

/s/ JOHN M. ENGLAND
John M. England
Receiver

JME/mjm
Enclosure

$13.55 O.D.

[fol. 11]

EXHIBIT "C" TO ANSWER

October 3, 1963

Mr. John M. England
155 Montgomery Street
San Francisco 4, California

Dear Mr. England:

In reply to your letter of October 2, the commercial account of Marin Seafoods, Inc. is presently overdrawn in the amount of $13.55. We would appreciate your check in this amount if possible.

Very truly yours,

B. R. Kirchner
Vice President

BRK:pla

[fol. 12]

EXHIBIT "D" TO ANSWER

SPECIALIZING AS
CREDITORS REPRESENTATIVE
RECEIVER AND TRUSTEE IN
U. S. BANKRUPTCY COURT

JOHN O. ENGLAND
JOHN M. ENGLAND
155 Montgomery Street
Room 601
San Francisco 4, Calif.

Phone GArfield 1-4327

October 14, 1963

Bank of Marin
836—4th Street
San Rafael, California

in re: MARIN SEAFOODS, INC.

Gentlemen:

I am in receipt of your letter of recent date regarding the over-drawn status of the account in the name of the above named bankrupt.

Please forward a copy of your statement covering activity on this account from the 26th day of September, 1963 if the original has already been mailed. If the original is in your files please forward this together with the checks paid. I am particularly anxious to know the dates and the amounts of deposits made after September 20, 1963.

Your prompt attention will be appreciated.

Very truly yours,

/s/ JOHN M. ENGLAND
John M. England

JME:egf

[fol. 12a]

IN THE UNITED STATES DISTRICT COURT

FOR THE NORTHERN DISTRICT OF CALIFORNIA

SOUTHERN DIVISION

No. 74820

In Bankruptcy

[Title omitted]

ANSWER TO APPLICATION FOR TURNOVER ORDERS
—Filed December 20, 1963

Eureka Fisheries Inc., a corporation, doing business as Eureka Seafoods, answers the application for turnover orders of the referee as follows:

1. Admit the allegations contained in paragraphs 1, 2 and 3.

2. Deny each and every, all and singular, generally and specifically the allegations contained in paragraph 4. Upon information and belief allege that the deposits of $604.30, $251.51, $503.72 and $892.04 were all made on September 26, 1963, and that the amounts of said deposits were not credited to the account of the said bankrupt until the dates of September 27 and September 30 as alleged in the application. Allege that the bankrupt, as cash payment for merchandise delivered by Eureka Seafoods to the bankrupt, did make, execute and deliver to Eureka Seafoods checks drawn upon the account of the bankrupt at the Bank of Marin, San Rafael, California, upon the commercial bank account No. 16-00139. Allege that Eureka Seafoods did present said checks to the bank for payment, but that the bank did refuse to make payment thereof and [fol. 12b] that Eureka Seafoods did thereupon deposit said checks with the bank for collection upon the very first monies deposited in the account of the bankrupt.

3. Admit the allegations contained in paragraph 5.

[File endorsement omitted]

4. Allege that Eureka Fisheries Inc., dba Eureka Seafoods, does not have any information with respect to the matters set forth in paragraph 6, and basing its denial upon this ground, denies each and every, all and singular, generally and specifically, the matters and facts alleged in paragraph 6.

5. As and for a further and separate defense Eureka Fisheries Inc., alleges that the relationship of the bank to its depositor is that of debtor and creditor and that the payment by the bank to Eureka Fisheries Inc., of monies as alleged in the application herein, is a payment by the bank of its own money, and does constitute a payment by the bank as an overdraft. Allege that Eureka Fisheries Inc., is not obligated in law to return the money so paid to it on an overdraft. Allege that the money so paid to Eureka Fisheries are not an asset of the estate in bankruptcy herein.

Wherefore, Eureka Fisheries Inc., dba Eureka Seafoods, prays that the referee and receiver receive nothing by the application on file herein.

Dated: December 17, 1963.

Mathews & Traverse, By Francis B. Mathews,
Attorneys for Eureka Seafoods Inc.

[fol. 12c] *Duly sworn to by L. R. Thomas, jurat omitted in printing.*

[fol. 12d] Affidavit of Service by Mail (omitted in printing).

[fol. 13] [File endorsement omitted]

[fol. 14]

IN THE UNITED STATES DISTRICT COURT

FOR THE NORTHERN DISTRICT OF CALIFORNIA

SOUTHERN DIVISION

No. 74820

In Bankruptcy

In the Matter of

MARIN SEAFOODS, INC., Bankrupt.

Before: Honorable Lynn J. Gillard, Referee in Bankruptcy.

HEARING ON TRUSTEE'S APPLICATION FOR TURNOVER ORDER —Friday, December 20, 1963

[fol. 15]

COLLOQUY BETWEEN REFEREE AND COUNSEL

The Referee: In the Matter of Marin Seafoods.

Mr. Block: That is ready, Your Honor.

Mr. Gill: That is ready, Your Honor.

Mr. Block: I might state to Your Honor that I do expect one other witness and that is Mr. England, but I think we can proceed at the present time without him.

There is on file, as Your Honor knows, an Application for Turnover Orders filed November 27, 1963. I have received pleadings from the Bank of Marin and also from Eureka Fisheries to the application, and I have also had the opportunity this morning of discussing those pleadings with counsel for the bank and counsel for Eureka Seafoods. With respect to the allegations—and I believe, Mr. Gill, I am correct, am I not—you are willing to stipulate that the deposits of $604.30, $251.51, $503.72, and $892.04 were all made as indicated in the application; is that correct?

Mr. Gill: Yes, it is.

The Referee: Let's have the appearances for the record.

Mr. Gill: For the record, my name is Walton Gill of Mathews & Traverse.

The Referee: Representing Eureka Fisheries?

Mr. Gill: Eureka Fisheries.

Mr. McCarthy: I am Bryan McCarthy, Your Honor. I am from the firm of Freitas, Allen, McCarthy & Bettini in [fol. 16] San Rafael, and I appear for the Bank of Marin.

Mr. Block: Also, the answer of Eureka Fisheries on page 2, paragraph 4, alleges that they have no information concerning the matters set forth in paragraph 6 of our application and they deny on that ground the allegations of paragraph 6:

> "That without the knowledge or consent of your applicant, said Bank of Marin did pay over unto Eureka Fisheries, dba Eureka Seafoods, on or about October 2, 1963, sums totaling $2,355.07."

Now, I think I am correct, am I not, counsel, in stating that there was an error in that calculation, that the total amount pay-over to the Eureka Fisheries was not $2,355.07 but $2,312.82?

Mr. Gill: That is correct. The petition for turnover order was to be reduced by $42.25.

Mr. Block: I might state, Your Honor, that in checking over the matter I noticed that the $42.25 was paid to one Andrew Bettini and not paid to Eureka Fisheries. So that you withdraw that answer to the application?

Mr. Gill: Yes, we do.

Mr. Block: Now, if Your Honor please, in respect—

The Referee: Well, the answer of Eureka Fisheries is that it has no knowledge with reference to paragraph 6. That is withdrawn, is that correct, and now there is an [fol. 17] admission that this amount, $2,312.82, was paid over to Eureka Fisheries?

Mr. Block: That is correct, on or about October the 2nd.

Now, if Your Honor please, with the pleadings in the state that they are, I might say that in my opinion the pleading of the bank presents—doesn't controvert any of the allegations made by the Trustee in this case and I believe that they may stand deemed admitted. There are no denials of those allegations.

Mr. McCarthy: In that regard, counsel, you mean they deem admitted that we don't admit we owe you any money, but just the factual situation?

Mr. Block: The factual situation is deemed admitted, and by the stipulation just received from Eureka Seafoods I think that the allegations are all taken as true, as well.

Mr. Gill: The factual situation, yes.

Mr. Block: So then basically, if Your Honor please, I believe that we have presented here this morning a matter of law.

Now, in that connection, it is the Trustee's position—

The Referee: Wait a minute. The deposits, you said, the first four deposits referred to in paragraph 4, are admitted by Eureka Seafoods, not the last four?

[fol. 18] Mr. Block: All the deposits totaling—that there were deposits made to the account representing the collection by the bankrupt officer to the account of Eureka Seafoods totaling the amount specified in the application. They are admitted. Is that correct, counsel?

Mr. Gill: Paragraph 4, yes.

The Referee: I gathered when you read off the amounts you merely read off the first four items.

Mr. Block: No. These are all admitted. The other figure, the $2,312.82, is the amount of the $3,182.09 that the Eureka Fisheries received from the bank on the collection being cleared on October the 2nd. In other words, there was deposited between September 27th and October the 8th a total to the account of the bankrupt of $3,182.09. Of that amount on October the 2nd, 1963, checks totaling $2,312.82 were honored by the bank and paid to Eureka Fisheries and Eureka Fisheries received that amount from these deposits.

Mr. McCarthy: Counsel, I am not representing Eureka Fisheries. I think, counsel, that if you will check these amounts, that unless these sums total this—

Mr. Block: Remember, I made mention that you deduct the $42.25.

$2,312.82.

Mr. McCarthy: $2,212.82.

Mr. Block: $2,312.82. I think counsel for the Fisheries [fol. 19] and I have both checked those figures and they are correct.

Now, with the pleadings—

The Referee: Maybe we had better go over it a little bit. The answer of the bank which I am looking at now indicates that—I see. The bank said there was no money in the bank on October 3rd.

Mr. Block: Yes.

Mr. McCarthy: That is correct. There was an over-draft of $13.55.

The Referee: This would be consistent with what the Trustee says. There was money prior to that time which was withdrawn on October 2nd.

Mr. McCarthy: Excuse me. It may be that the photostat attached left out a thing. It should have the letters "OD" after that. It shows in red and black on the original.

The Referee: I see what you mean. Counsel indicates that in Exhibit A attached to his answer the balance for October 2nd is an over-draft. There is a minus balance.

Mr. McCarthy: You might put "OD" there. In the photostat it was just missed in the figures being in red which indicates it was an over-draft.

Mr. Block: Your Honor, the pleadings as indicated and the stipulations as indicated, I would like at this time [fol. 20] to make a motion to strike both of the answers and ask for a summary judgment or judgment on the pleadings in favor of the Trustee for this reason: Section 70(a) of the Bankruptcy Act provides that the Trustee obtains title to all property, with certain minor exceptions, as of the date of the filing of the petition in bankruptcy. It is admitted by the pleadings that the bankrupt's petition was filed on September the 26th, 1963. The property of the bankrupt, as of that date, wherever it was or wherever it was located, became the property in custodia legis of this court and the Trustee takes title to all property as of the date of the filing of the petition. There are certain instances, as Your Honor well knows, where payments made or property dispersed after the bankruptcy are protected. Those items are specified very clearly in Section 70(d) of the Bankruptcy Act which states:

> "After bankruptcy and either before adjudication or before a receiver takes possession of the property of the bankrupt, whichever first occurs—"

And then it lists five types of transactions that are protected. This is the only protection accorded by the Bankruptcy Act; and Your Honor will notice that the very first paragraph of that section 70(d) lists two dates. It says: "Either before adjudication or before a receiver takes possession."

[fol. 21] This action is admittedly a voluntary petition in bankruptcy and a voluntary petition in bankruptcy under Section 18(f) of the Bankruptcy Act operates "as an adjudication with the same force and effect as a decree of

adjudication." That being the situation, it is the Trustee's contention and position that Section 70(d), the only section in the Bankruptcy Act that protects transactions occurring subsequent to a bankruptcy petition does not apply in the case of a voluntary petition in bankruptcy. That being the case, there isn't any question but that upon the pleadings the Trustee is entitled to recover the full amount of the deposits made subsequent to the bankruptcy.

Now, the only other issue—

The Referee: Is it your contention that the Trustee has the right of collection against each of the named respondents?

Mr. Block: Yes, Your Honor. I think that that is so. Frankly, my position is that I believe the primary obligation is on the bank in this situation. However, equitably speaking, I know that the Eureka Fisheries received a substantial portion of this money and for that reason I thought equitably they should appear before the court and it may be that the equitable solution is to charge the party who received the benefit of these monies that did in fact belong to the Trustee in the amount so received and let [fol. 22] them amend their claim accordingly and increase it accordingly and charge the bank with the balance of the deficiency.

The Referee: What happened to the balance of the money that is alleged deposited after bankruptcy and not paid out to Eureka Fisheries?

Mr. Block: Well, Your Honor, one item, the bank did pay $168.80 to Mr. England on October 17th.

The Referee: I see that allegation. I presume that is admitted?

Mr. Block: Credit has been given in the calculations made. There was another sum of $149.25 which was paid to a man by the name of Hugh Bourne. Possibly he should be brought in, but he is not presently before the Court. There is another item of $42.25 paid to Andrew Bettini. There is another item here of $4.47 service charges. No issue is being made on those items.

There is another item of $126.70 also paid to Mr. Hugh Bourne subsequent to the bankruptcy and a $73.24 item to Crocker; and a $16.50 item to the Bay Area Transfer Warehouse. There is one item here of $107.98. What is this, Mr. England?

Mr. England: Bourne and Bettini are wage claims which conceivably could be priority.

Mr. Block: There is another item here of $107.98 and a couple of other items on the statement of $2.00 apiece. [fol. 23] Those are not in issue between the parties before Your Honor at this moment.

The Referee: All right. There is only one other question I have to ask of Mr. Block. Your first statement was, you asked that the answer be stricken and then you asked for judgment on the pleadings. I think the two requests are mutually exclusive.

Mr. Block: Well, if the pleadings of the respective respondents are stricken from the record as being non-responsive to the issues involved, then it would appear to me—

The Referee: Well, they are responsive in the sense that you have an admission of the facts upon which you base your request for a summary judgment, I guess, or judgment on the pleadings. Judgment on the pleadings requires that the pleadings be considered, I assume.

Mr. Gill: Your Honor, our position in connection with this—

The Referee: First let me ask you: Is it correct and also, Mr. McCarthy, is it correct that there is no factual issue, that the pleadings and the stipulations which have been entered here this morning disclose the situation basically as alleged in the petition and that we have no factual matters to be determined by the Court?

Mr. Gill: I feel that there are no factual matters.

[fol. 24] Mr. McCarthy: I feel there aren't, as long as the facts set forth in my answer are also considered as true, none of which are contradictory.

Mr. Block: No. I don't dispute the facts as such filed by the Bank of Marin, except that I say that they are irrelevant to the issues involved here. What they say there may be true, but in effect I demur to them not having any legal effect so far as the Trustee's right to the money is concerned.

In other words, whether they had notice of the bankruptcy or not is irrelevant here and in a voluntary petition in bankruptcy the adjudication is immediate and title passes immediately to the custody of the court. It used to be different many years ago when there was a hiatus period between the filing of a voluntary petition and the actual adjudication. In the old days before the amendment of the statute, the adjudication might come some period of time subsequent to the filing of the petition in bankruptcy and it was that hiatus period that may have been protective; but it is no longer protected and, as a matter of fact, you would have to guess as to when it would normally be made. Here the adjudication is automatic on the date of the filing, to wit, on the 26th of September.

The Referee: Is there a section specifically with reference to banks or is 70(d) the only one?

[fol. 25] Mr. Block: 70(d) is the only section I have been able to find where certain transactions are protected in bankruptcy situations and Your Honor will note that under Section 70(d), even when they qualify under Section 70(d), that the burden of proof transfers to the party claiming the right to have this protection.

The Referee: I guess I was thinking about there is a right of a setoff for a banker's lien subsequent to bankruptcy. Is that the only specific post-bankruptcy situation you can think of?

Mr. Block: That is right, Your Honor. There is such a protection to the banks where the banks have loaned money. They can always offset.

The Referee: All right, Mr. Gill.

Mr. Gill: Your Honor, our basic position is set out in part in paragraph 5 of our answer. The point is that we

feel that the bank is in a relationship to their depositor, Marin Seafoods, the bankrupt, of a debtor and creditor.

As of the date of the bankruptcy, and thereafter, because of these deposits, the bank owed the bankrupt, or the Trustee, as the case may be, some money. However, the money in this particular case is not in specie but a debt only, and we haven't received the money therefor of the bankrupt. We have received the money of the bank and as such we feel that we are not obligated to the Trustee. [fol. 26] Frankly, we feel that if the Trustee has any claim, it is against the bank, which we term as a debtor of the bankrupt. We are in a position similar to a person who has been paid on an over-draft by a bank, without the consideration of the bankruptcy. The bank's problem is with us. If it is an over-draft or, in this case, payment out of funds that the bank should have paid to someone else, we feel that under these circumstances that we are not in any way obligated to the Trustee and our relationship is solely with the bank.

As Mr. Block says, it may be equitable to bring us in here. I don't think we are dealing with the matter of equity in this particular instance. I think we are dealing strictly with the matter of the debtor-creditor relationship. Therefore, I don't think we have any obligation at all to the Trustee.

The Referee: I think all that he was referring to, if I understood his remarks, that as far as he was concerned, it was equitable, in view of the bank's situation, to bring you in because you received the money and the bank didn't. I think that is all that was intended to be implied. I don't think there was any attempt by that to change the legal situation, but merely to indicate that he assumed that the bank is fully responsible, that you got more benefit from the money than the bank did, and therefore you are here, I gather.

• • • • • • •

[fol. 37]

IN THE UNITED STATES DISTRICT COURT

FOR THE NORTHERN DISTRICT OF CALIFORNIA

SOUTHERN DIVISION

No. 74820

In Bankruptcy

[Title omitted]

MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT OF TRUSTEE'S APPLICATION FOR TURNOVER ORDERS—Filed December 30, 1963

From the pleadings on file herein, and from the stipulations made in open court at the time of the hearing on this matter, the facts of this case are as follows:

On September 26, 1963, Marin Seafoods, Inc., a corporation, filed its voluntary petition in bankruptcy. At the time of the filing of such voluntary petition in bankruptcy, there was due and owing from customers of said bankrupt monies for merchandise previously delivered by the bankrupt to said customers, the amount of said accounts receivable being in excess of $3,200.00. The bankrupt's principal officers thereupon collected a total of $3,182.09, of such accounts receivable, and deposited those funds in its bank account at the Bank of Marin, all of said deposits being made subsequent to the filing of the bankruptcy [fol. 38] petition. Prior to bankruptcy, the bankrupt herein had issued a series of checks to Eureka Fisheries totaling $2,312.82. These outstanding checks were honored by the bank on October 2, 1963, and charged against the deposits then in the hands of the bank. Additionally, the bank honored other outstanding checks, totaling $700.47, in favor of other creditors, such checks, likewise, being out-

[File endorsement omitted]

standing at the time. The bank did not receive actual notice of the bankruptcy until October 3, 1963.

Issues

1.) Is the bank liable to the trustee for the deposits made by the bankrupt subsequent to the filing of its voluntary petition in bankruptcy, despite its lack of actual knowledge of the existence of the bankruptcy proceeding; and

2.) Is Eureka Fisheries liable to the trustee in bankruptcy to the extent that checks in its favor were honored by the bank under the circumstances recited?

Argument

With respect to the first issue, it is the trustee's position that the bank is chargeable with the full amount of the deposits made by the bankrupt officer to the bankrupt's bank account subsequent to bankruptcy in the sum of $3,182.09, and the fact that the bank had no actual notice of the bankruptcy until October 3, 1963 is completely irrelevant.

The trustee's position is supported by Section 70(a)(5) of the *Bankruptcy Act* which provides (so far as the same is relevant here) as follows:

> "The trustee of the estate of a bankrupt . . . upon his . . . appointment and qualification, shall . . . be vested by operation of law with the title of the bankrupt as of the date of the filing of the petition initiating a proceeding under this Act, . . . to all . . . (5) property . . . which prior to the filing of the petition he could by any means have transferred . . . "

[fol. 39] The above quoted section of the Bankruptcy Act is interpreted as follows:

> "The title of the bankrupt vests in the trustee 'as of the date he was adjudicated a bankrupt,' but upon

thus vesting relates back to the time of the filing of the petition. While it is true that by subsection 'a' the trustee, upon his appointment and qualification, becomes vested by operation of law with the title of the bankrupt as of the date he was adjudged a bankrupt, there are other provisions of the statute which evidence the intention to vest in the trustee the title to such property as it was at the time of the filing of the petition, the estate being considered as 'in custodia legis' from that time."

Collier on Bankruptcy, Vol. 4, Section 70.05, p. 963.

If it be contended here that the deposits made by the bankrupt corporation to its bank account subsequent to bankruptcy constitute "after-acquired property" not passing to the trustee in bankruptcy, the answer to that question is contained in *Collier on Bankruptcy,* Vol. 4, Section 70.09, p. 999:

"Accordingly, it has been stated that 'money or other property which is the proceeds of property owned by the bankrupt at the time the petition was filed is not after-acquired and vests in the trustee.' "

With respect to the specific matter of deposits made to a bank account, *Collier on Bankruptcy,* Section 70.31, at pp. 1282-83, states as follows:

"Deposits in a bank to the credit of a bankrupt pass to the trustee as assets of the estate. Thus where through delay a check drawn on such a deposit prior to bankruptcy is presented and paid after bankruptcy, the payee is not entitled to retain the sum received as against the trustee."

See also the matter of *Tele-Tone Radio Corporation* (D.N.J. 1955) 133 Fed. Supp. 739.

In certain instances, however, persons receiving property or money from the bankrupt subsequent to bankruptcy are protected. See Section 70(d) of the *Bankruptcy Act*. [fol. 40] This protection, however, is accorded only during a specific time interval, if such time interval does, in fact, exist. Section 70(d) of the *Bankruptcy Act* (so far as is relevant here) delineates this time interval as follows:

> "After bankruptcy and either *before adjudication* or before a receiver takes possession of the property of the bankrupt, *whichever first occurs*" is the time limit so specified. (Emphasis supplied.)

Section 70(d) then describes certain limited situations wherein persons receiving money or property from the bankrupt may be protected during such limited time interval.

Interrelated with Section 70(d) is Section 18(f) of the *Bankruptcy Act* which provides as follows:

> "The filing of a voluntary petition under Chapter I to VII of this Act, other than a petition filed in behalf of a partnership by less than all of the partners, shall operate as an adjudication with the same force and effect as a decree of adjudication."

Accordingly, where, as here, a voluntary petition in bankruptcy is filed on September 26, 1963, the adjudication is automatic; there is no time interval whatsoever. In such circumstances, the bank may not utilize Section 70(d) as a defense. Whether or not it had actual knowledge of the proceeding is irrelevant; the filing of a voluntary petition in bankruptcy is a caveat to all the world. The corollary to this proposition is, of course, that Section 70(d) of the *Bankruptcy Act* is not applicable where a *voluntary* petition in bankruptcy has been filed, as is the case here.

This position is strengthened by Section 70(d)(5) which contains the following additional language:

"Except as otherwise provided in this subdivision and in subdivision (g) of section 21 of this Act, no transfer by or in behalf of the bankrupt after the date of bankruptcy shall be valid against the trustee."

[fol. 41] See *Collier on Bankruptcy,* Section 70.68, p. 1503, which reads:

"The clear implication of subdivision (d) is that any payment of indebtedness owing the bankrupt or any delivery of his property that is not authorized by clause (2) is invalid against the trustee."

It is clear, therefore, that the deposits made by the bankrupt to its bank account subsequent to bankruptcy, and totaling the sum of $3,182.09, constitute property belonging to the trustee herein. The bank has paid to the trustee the sum of $168.80 of such funds, and is, accordingly, liable to the trustee herein for the difference, to-wit: the sum of $3,013.29.

With respect to the second issue involved in this case, the same being whether or not Eureka Fisheries is liable to the trustee herein for the benefit it received subsequent to bankruptcy, it must necessarily follow that Eureka Fisheries is liable at least to that extent. Certainly, this proposition is true on equitable grounds. Eureka Fisheries is in a position to amend its claim previously filed herein to the extent that it is required to reimburse the trustee for monies it received that rightfully belong to the trustee in bankruptcy.

If the bank itself is held solely responsible for the entire amount of the deposits made subsequent to bankruptcy, there is, of course, the possibility that the bank may have a cause of action for money paid by mistake to Eureka Fisheries. However, so far as the present case is concerned, this matter need not be decided by this court.

In this connection it is interesting to note the case of *In Re Autocue Sales & Distributing Corp.* (U.S. Dis. Ct.

—S.D. New York, 1958) 162 Fed. Supp. 17, which case, it is noted, is not relevant here since it involved the issue of whether or not Section 70(d) of the *Bankruptcy Act* protected certain persons who asserted they had no knowledge [fol. 42] of the bankruptcy proceeding.

Under the circumstances present in our case, of course, the trustee could have proceeded against those individuals who paid the accounts receivable to the bankrupt corporation subsequent to bankruptcy, and the fact that prior payment was made would not accord them protection either. See also *Kohn* v. *Meyers* (U.S. Ct. of Appeals, 6th cir.—1959) 266 Fed. (2nd) 353.

It is, therefore, respectfully submitted that the trustee herein is entitled to a turnover order against the bank requiring it to reimburse the trustee to the extent of $3,013.29; or, alternatively, that Eureka Fisheries be directed to turn over to the trustee herein the sum of $2,312.82, and that the Bank of Marin be directed to turn over to the trustee herein the further sum of $700.47.

Dinkelspiel & Dinkelspiel, By: Harold A. Block,
Attorneys for Trustee.

[fol. 42a]

IN THE UNITED STATES DISTRICT COURT

FOR THE NORTHERN DISTRICT OF CALIFORNIA

SOUTHERN DIVISION

No. 74820

In Bankruptcy

[Title omitted]

POINTS AND AUTHORITIES OF EUREKA SEAFOODS INC.
—Filed January 10, 1964

Primarily we would like to distinguish several of the cases cited by the attorneys for the Trustee.

In the Tele-Tone Radio Corporation case, 133 Fed Supp 739, the holder of the check had not yet received his monies from the bank and the question was whether the check operated as an assignment of the funds on deposit. The Court quite properly ruled that it did not operate as an assignment of monies on deposit although the court did not expressly state that the relationship of debtor and creditor exists between the bank and its depositor, its decision is predicated upon such a line of reasoning and such is impliedly stated in his ruling that the check does not operate as an assignment of the monies on deposit.

The In Re Autocue Sales & Distributing Corp, 162 Fed Supp 17, is a case which does not appear to have any relevancy at all of the situation presently before us. It is not a check situation and although it is referred to (page 5 of the trustee's brief) as a holding in connection with persons who had no knowledge of the bankrupt proceedings, the court expressly finds that they did have knowledge of the bankruptcy proceedings.

[File endorsement omitted]

With respect to the relationship of the bank and its depositor, there are three cases that expressly hold that [fol. 42b] the relationship is that of debtor and creditor. Burton v U.S. 196 US 283, 49 LEd 482, 488; In Re Kountz Bros. 104 F2d 157; In Re Ruskay 5 F 2d 143. These cases are all authority for the proposition that the relationship between the bank and a depositor of funds is that of a debtor and creditor relationship so that the trustee has a claim only against the bank and does not have a right against specific funds. Any problem of the bank and Eureka Seafoods Inc., must be resolved by separate litigation by the bank and Eureka Seafoods Inc.

It is respectfully submitted that the Honorable Referee should rule that the Trustee has a claim only against the bank and not against Eureka Seafoods Inc.

Mathews & Traverse, by: Francis B. Mathews,
Attorneys for Eureka Seafoods Inc.

[fol. 42c] Affidavit of Service by Mail (omitted in printing).

[fol. 43]

IN THE UNITED STATES DISTRICT COURT

FOR THE NORTHERN DISTRICT OF CALIFORNIA

SOUTHERN DIVISION

No. 74820

In Bankruptcy

[Title omitted]

MEMORANDUM OF POINTS AND AUTHORITIES OF RESPONDENT, BANK OF MARIN—Filed January 31, 1964

Facts

On September 26, 1963, Marin Seafoods, Inc., a corporation, filed its voluntary Petition in Bankruptcy. Thereafter, on October 3, 1963, the Bank of Marin received the first notice of any kind of the bankruptcy proceeding in the form of a letter from the Trustee, John M. England.

Prior to receiving the letter on October 3, 1963, as set forth above, the Bank of Marin received various deposits from the Marin Seafoods, Inc. and honored certain checks drawn upon the account of Marin Seafoods, Inc. (See Exhibits "A", "B", "C" and "D" attached to Answer of this respondent for the bank statement and the letter.)

The letter received on October 3, 1963, by the Bank of Marin, as referred to above, was dated October 2, 1963, and requested that the Bank forward a check for the present balance on deposit in the Bank of Marin in the name of the Marin Seafoods, Inc. On the date that the Bank received said letter, Marin Seafoods, Inc. was in fact over-[fol. 44] drawn, and the Bank so notified the Trustee. The Trustee's letter of October 2, 1963, made no reference and

[File endorsement omitted]

did not request that the Bank of Marin forward to the Trustee any further sums deposited in the account of Marin Seafoods, Inc.

After October 3, 1963, the Bank of Marin received further deposits from Marin Seafoods, Inc., and honored several further checks drawn upon its account. On October 17, 1963, the Bank of Marin received a second letter from the Trustee herein, under the date of October 14, 1963, requesting that the Bank forward a statement covering the account of Marin Seafoods, Inc.

At no time prior to October 3, 1963, did the Bank of Marin have any notice of the bankruptcy proceedings herein and at no time did the Bank of Marin receive an order of any nature concerning after-received funds sent to the Bank of Marin by the Marin Seafoods, Inc. Subsequent to the receipt of the letter of October 14, 1963, from the Trustee, the Bank of Marin forwarded the then balance of the Marin Seafoods, Inc. account to the Trustee, in the sum of $168.80.

Issue

Is the Bank of Marin liable to the Trustee herein for checks honored by it subsequent to the filing of the voluntary Petition in Bankruptcy in spite of its lack of actual knowledge of the existence of the bankruptcy proceedings?

Argument

I.

A Bank is not liable when in good faith and without actual knowledge of the bankruptcy proceedings it honors the bankrupt's checks in the regular course of its business after the adjudication of bankruptcy. *Rosenthal* v. *Guaranty Bank and Trust Co.* (D.C. La. 1956) 139 F. Supp. 730.

Briefly, the facts of the *Rosenthal Case, supra,* are as follows: On October 3, the bankrupt filed a voluntary petition for corporate reorganization under Chapter X of the

Bankruptcy Act, 11 U.S.C. Sections 501-676 (1952), in a [fol. 45] Federal District Court in New York. The petition was approved by Order of Court the same day. Approval of a Chapter X petition is equivalent to an adjudication of bankruptcy for the purpose of applying the provisions of Chapters I through VII of the Bankruptcy Act. Bankruptcy Act Section 102; 11 U.S.C. Section 502 (1952). Subsequently, from October 4 to October 10, the defendant a Louisiana bank, paid checks amounting to approximately $7,000.00 drawn upon it by the bankrupt. The Court found as a fact that the bank had no "actual knowledge" of the bankruptcy proceedings until formal notice was received from the Trustee on October 11. This action was one by the Trustee against the bank to recover the sum of $7,000.00. The Court held that there was no liability on the part of the bank.

The Court based its decision upon Bankruptcy Act Section 70d(5) (11 U.S.C. Section 110d (5)) which states:

> "A person asserting the validity of a transfer under this subdivision shall have the burden of proof. Except as otherwise provided in this subdivision and in subdivision (g) of Section 44 of this title, no transfer by or in behalf of the bankrupt after the date of bankruptcy shall be valid against the trustee; *provided, however, that nothing in this title shall impair the negotiability of currency or negotiable instruments.*"

The Court then stated that one of the purposes of the negotiability clause as it appears in Subparagraph (5) of subdivision d, Section 110, Title 11 U.S.C.A. is to protect banks who in good faith, for present equivalent value, in the usual course of their business, and without actual knowledge of the bankruptcy, honor checks drawn upon it by the bankrupt. (*Rosenthal* v. *Guaranty Bank and Trust Company, supra,* at page 736.)

The policy behind the holding of the *Rosenthal Case, supra,* has been set forth on numerous occasions in cases

cited prior to the 1959 amendment to Bankruptcy Act Section 18 (g) (now Bankruptcy Act Section 18 (f),) which amended the act so that the filing of a voluntary petition constituted an automatic adjudication of bankruptcy. Prior to the amendment, the law required the District Judge to hear all voluntary petitions and to make the adjudication or dismiss the petition. These earlier cases uniformly held that the bank, after the filing of the petition in bankruptcy, without actual notice of the filing of the petition, may, prior to [fol. 46] actual adjudication, receive deposits from the bankrupt to the credit of the latter's checking account and may make payments therefrom to third persons upon the depositor's checks without incurring liability from the Trustee in bankruptcy. This was so even though the eventual adjudication of bankruptcy was deemed to take place at the time of the filing of the petition under the doctrine of relation-back set forth in the Bankruptcy Act.

Citizens National Bank v. *Johnson* (6th Cir. 1923) 286 F. 527

Matter of Retail Stores Delivery Corp. (D.C. N.Y.) 11 F. Supp. 658;

Matter of Zotti (2nd Cir.) 186 F. 84, cert. den. 223 U.S. 718, 32 S. Ct. 522, 56 L. Ed. 628.

The reasoning of these cases can best be summarized by the following quotations:

"A bank is not liable when, in good faith, in the ordinary course of business, it pays checks drawn by a concern against which, unknown to the bank, a petition in bankruptcy has been filed, with no restraining order outstanding and prior to adjudication. Most of these cases base the denial of a turnover order upon the ground that the bank in question was unaware that a petition in bankruptcy has been filed, and it was held that under such circumstances it would be inequitable

and impractical to make the bank refund to the trustee the amount of such checks paid by it; otherwise, a bank could never pay a check without first ascertaining whether a petition in bankruptcy had been filed against the one who drew the check." (*Matter of Retail Stores Delivery Corp.* (D.C. N.Y.) 11 F. Supp. 658, at 659.)

"Its effect would be that the bank could not protect itself against liability to a trustee in bankruptcy subsequently appointed on account of payments made in good faith and in the regular course of business and in ignorance of the bankruptcy proceedings—except through the impossible course of keeping itself advised, not only daily, but momentarily, of the filing of petitions for adjudication of bankruptcy against its depositors in any competent jurisdiction. . . . True, broadly speaking, the adjudication when made relates back to the commencement of the bankruptcy proceedings for the purpose of adjudicating rights and equities generally. But we think that both on principle and authority the rule referred to does not make the banks liable for good faith payments to third persons made before adjudication upon depositors' checks in the regular course of business and without knowledge or notice of bankruptcy." (*Citizens National Bank* v. *Johnson* (C.C.A. 6th Cir.) 286 F. 527).

The reasoning set forth in the above quotations is equally applicable to the fact situation involved herein as it was to the facts dealt with in the cases decided prior to the 1959 amendment to Bankruptcy Act Section 18(g). [fol. 47] Consequently, under the authority of the *Rosenthal Case, supra,* the Bank of Marin is not liable to the Trustee herein for checks honored by it prior to its receiving actual notice of the bankruptcy proceedings on October 3, 1963, in spite of the fact that the petition in bankruptcy had been previously filed.

The authorities cited in the Memorandum of Points and Authorities in support of Trustee's application for turnover orders are not in point and uniformly beg the question. The issue is not whether the Trustee is vested by operation of law or otherwise with the title of the bankrupt as of the date of the filing of the petition, but it is whether or not there is any liability on the part of the Bank of Marin under the factual situation herein. Both reason and the authorities hold that there is no such liability.

II.

Second, the Bank of Marin is not subject to summary proceedings of the Bankruptcy Court and may not be compelled by means of a turnover proceeding to reimburse the Trustee for the sums that it paid to third party payees pursuant to checks drawn by the bankrupt herein. *In re Fuller* (C.C.H. 2d Cir. 1923) 294 F. 71.

The relationship of the depositor and the bank is that of a debtor and creditor. It is the general obligation of the bank to honor its depositor's checks. *In re Retail Stores Delivery Corp.* (D.C. N.Y. 1935) 11 F. Supp. 658.

Consequently, a bank holding deposits of a bankrupt, part of which are claimed by a payee of a check issued by the bankrupt after the petition had been filed against him, is an "adverse claimant" as such is defined in Bankruptcy Act Section 23 (11 U.S.C. Section 46) and as a result, is not subject to a summary order to pay over the entire deposits to the Trustee in bankruptcy. *Collier on Bankruptcy,* Section 23.06 (8); *In re Fuller* (C.C.A. 2d Cir. 1923) 294 F. 71.

In the *Fuller Case, supra,* the Court held that:

> "Banks holding deposits are debtors, and ordinarily are adverse claimants, not subject to summary jurisdiction. If there is a substantial basis for an adverse

claim, and such is not merely colorable, the claimant must be remitted to adjudicate his claim in a plenary suit." (at page 73.)

[fol. 48] The rule has long been settled that a Trustee to succeed in capturing summarily property held by a third party, must be able to show from facts which no fair mind can dispute, that the claim to the property so held is so insubstantial and obviously insufficient in either fact or in law as to be plainly without color of merit or a mere pretense. If there is substance to the claim, the Trustee must proceed in a plenary suit. *In re Indiana Flooring Company* (C.C.A. 2d Cir. 1933) 62 F. 2d 763. There has been no showing herein that the claim of the Bank of Marin is anything but meritorious in both fact and in law, and consequently, under the above cited authorities, the Bank is not subject to summary jurisdiction.

In conclusion, the respondent Bank of Marin should not be required to turn over any funds paid out prior to actual notice under the law of either ground above stated.

Respectfully submitted,

Freitas, Allen, McCarthy & Bettini, Attorneys for Bank of Marin.

[fol. 49] Proof of Service by Mail (omitted in printing).

[fol. 50]

IN THE UNITED STATES DISTRICT COURT

FOR THE NORTHERN DISTRICT OF CALIFORNIA

SOUTHERN DIVISION

No. 74820

In Bankruptcy

[Title omitted]

TRUSTEE'S ANSWER TO RESPONDENTS' MEMORANDUM OF POINTS AND AUTHORITIES—Filed February 14, 1964

Respondent Bank of Marin has argued that it should not be held liable to the trustee in bankruptcy when, after adjudication and before actual notice of bankruptcy, the bank honored the bankrupt's checks. As support for this proposition, respondent cites *Rosenthal* v. *Guaranty Bank & Trust Co.*, 139 F. Supp. 730 (W.D.La. 1956), where the court held that a bank was not liable to the trustee when, in the regular course of business, in good faith and without actual knowledge of bankruptcy, it honored the bankrupt's checks drawn prior to the filing of the petition. *Collier on Bankruptcy*, Sec. 70.68, at p. 1503, notes that the Rosenthal decision rests primarily on an erroneous application of the "negotiability" proviso of Sec. 70d(5) and comments:

> "The intimation that a purpose of the negotiability clause of Sec. 70d(5) is to protect banks which cash checks upon them drawn by bankrupts is surely with-
> [fol. 51] out foundation. The intention to protect banks cashing checks in good faith before adjudication or the appointment of a custodial officer is clear, but drawee banks are given no special position in that regard. . . . To charge a depositary bank with liability for cashing checks of its depositor after his adjudication does not

[File endorsement omitted]

impair the negotiability of the checks. Delivery of a check to the drawee bank for payment is not negotiation."

Respondent Bank of Marin's defense must fail because it is based on the same erroneous application of Section 70d(5).

The issue in this turnover proceeding is whether the bank is liable to the trustee for disbursing the bankrupt's post-adjudication deposits. The general rule is that "no transfer by or on behalf of the bankrupt after the date of bankrupty shall be valid against the trustee." *Bankruptcy Act*, Sec. 70d(5). Unless respondent can demonstrate that an exception is applicable in this case, the general rule must govern. The only provision remotely helpful to respondent is Sec. 70d(2) providing that *before adjudication* a "person indebted to the bankrupt or holding property of the bankrupt may, if acting in good faith, pay such indebtedness or deliver such property, or any part thereof, to the bankrupt or upon his order, with the same effect as if the bankruptcy were not pending . . ." This section provides limited protection to parties dealing with the bankrupt *prior to adjudication* and in good faith and, to some extent, permits a bankrupt to continue normal commercial activities. But Congress had to draw the line somewhere between these desirable commercial ends and the need to preserve a bankrupt's estate for the benefit of his creditors. Under those circumstances, Congress, through Section 70d of the Bankruptcy Act, fixed the *limit* of protection at the point of adjudication and decided that after that time, the limited protection available to parties dealing with the bankrupt should cease. For that reason, respondent having disbursed [fol. 52] the bankrupt's funds *subsequent to adjudication*, is not entitled to any exception from the general rule and, accordingly, is liable to the trustee.

Secondly, respondent Bank of Marin argues that it is not subject to *summary proceedings* for a turnover order to reimburse the trustee for the sums that it paid to third party payees pursuant to checks drawn by the bankrupt.

In this regard, respondent relies on *In re Fuller*, 294 Fed. 71 (2nd Cir. 1923). That case, however, involved deposits by the bankrupt *prior* to the filing of an involuntary petition in bankruptcy. The instant case is different. Here, the bankrupt had outstanding accounts receivable at the time he filed his *voluntary* petition. After filing, which under Section 18f operates as an automatic adjudication, the bankrupt collected some of its accounts receivable and deposited the resulting funds with the Bank of Marin. Hence, the bank's claim to the funds did not arise until *after adjudication*. Under these circumstances, the bankruptcy court unquestionably is authorized to resolve the controversy in a summary proceeding. This question was resolved in *In the Matter of Autocue Sales & Distributing Corp.*, 162 F. Supp. 17, 20 (S.D.N.Y. 1958) where the court said:

> "It is true that, where the controversy is with respect to property transferred before the filing of the petition, the bankruptcy court must, before it can hear the controversy in a summary proceeding, make a preliminary inquiry to determine whether the adverse claim is substantial or merely colorable. Once the petition is filed, however, the trustee is vested with title to all property in the possession of bankrupt, section 70(a) 11 U.S.C., Sec. 110(a), and the bankruptcy court has summary power to determine controversies with respect to property transferred after that date irrespective of the substantiality of the transferee's claim. Since, in this case, the bankrupt had undisputed possession of the accounts receivable at the time of the filing of the petition and title to that property had vested in the trustee as of that time, the controversy as to the subsequent transfer was properly determined in a summary proceeding."

[fol. 53] In view of the *Autocue* decision, it is clear that the normal relationship between a depositor and his bank is not controlling as to property that was in the hands of

the bankrupt at the time the petition in bankruptcy was filed. Since the bankrupt did not deposit the funds in issue in this proceeding until after the petition had been filed, a summary proceeding is proper.

In re Indiana Flooring Co., 62 F. 2d 763 (2d Cir. 1933), does not support respondent bank's claim that a plenary suit is required in the instant case, for that case involved a claim to property in the possession of a third person claiming title and possession at the time of the filing of the bankruptcy petition. Unlike a third party claiming an adverse interest as in *Indiana Flooring*, the Bank of Marin did not acquire any interest in the assets in question until *after adjudication*. The factual distinction is crucial in light of the court's decision in *Autocue*. Moreover, respondent bank, not having raised the summary jurisdiction issue at the onset, has waived the issue. Bankruptcy Act, Sec. 2a(7); F.R.C.P. Rule 12(h).

Respondent Eureka Seafoods, Inc., claims that the *Autocue* case is irrelevant to the present case. Although we conceded in our Memorandum of Points and Authorities that *Autocue* was not dispositive of any issue argued in the Memorandum, it clearly is dispositive of the summary jurisdiction question raised for the first time by the Bank of Marin in its Memorandum of Points and Authorities.

The assertion of Eureka Fisheries that the trustee has a claim only against the bank and not against Eureka Fisheries is not supported by any case cited for that proposition. *Burton* v. *United States*, 196 U.S. 283 (1905), involved only a factual question of whether a defendant located in Washington, D.C., had accepted payment on a check drawn on a St. Louis bank in Washington or St. Louis. *In re Kountze Bros.*, 104 F. 2d 157 (2d Cir. 1939), involved a [fol. 54] post-bankruptcy claim to funds deposited with the bankrupt several months before bankruptcy. In *In re Ruskay*, 5 F. 2d 143 (2d Cir. 1925), the question was whether a trust company became a debtor of the depositor at the time the deposit slip was prepared or at the time the trust company entered the deposit on its books.

In each case cited the court mentions the debtor-creditor relationship between bank and depositor, but none of the cases involves the question of transfers of the assets of the bankrupt after adjudication. On the other hand, under Section 70d(5) of the Bankruptcy Act it is clear that the trustee has a claim against Eureka Fisheries, the recipient of the transfer, as well as the Bank of Marin, the transferor.

For these reasons, it is submitted that neither respondent has demonstrated any basis for denial of a turnover order in this proceeding, and it is respectfully requested that the turnover orders requested in our Memorandum of Points and Authorities be granted.

Feb. 12, 1964

Dinkelspiel & Dinkelspiel, Harold A. Block, Attorneys for Trustee.

[fol. 54a] Proof of Service by Mail (omitted in printing).

[fol. 55]

IN THE UNITED STATES DISTRICT COURT

FOR THE NORTHERN DISTRICT OF CALIFORNIA

SOUTHERN DIVISION

No. 74820

In Bankruptcy

In the Matter of

MARIN SEAFOODS, INC., Bankrupt.

OPINION FOR ORDER—February 24, 1964

Title to the property of a bankrupt vests in the trustee as of the date of the bankruptcy petition pursuant to the

provisions of §70a of the Bankruptcy Act. Certain transactions thereafter but prior to adjudication are protected by §70d. However the statute places "an absolute ban on all transfers not given specific protection under the act". Feldman v. Capitol Piece Dye Works, Inc. (C.A. 2, 1961) 293 F. 2d 889.

No provision contained in §70d gives any protection to a bank which after adjudication honors the checks of the bankrupt. And the recipient of such funds after adjudication merely holds property title to which is vested in the trustee.

The bank on brief questioned the summary jurisdiction of the bankruptcy court. The point is belatedly raised. Bankruptcy Act §2(7). In any event the facts do not show the bank ever had any claim to these funds deposited with it after adjudication of the bankrupt.

[fol. 56] The trustee is entitled to a judgment against the Bank of Marin for $700.47 and against the Bank of Marin and Eureka Fisheries, jointly, for $2,312.82.

The trustee shall serve and lodge appropriate findings of fact, conclusions of law and order.

Dated at San Francisco, California, this 24th day of February, 1964.

Lynn Gillard, Referee in Bankruptcy.

[File endorsement omitted]

[fol. 57]

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF CALIFORNIA
SOUTHERN DIVISION

No. 74820

In Bankruptcy

[Title omitted]

FINDINGS OF FACT AND CONCLUSIONS OF LAW ON APPLICATION OF TRUSTEE FOR TURNOVER ORDERS—March 31, 1964

The above-entitled matter having come on for hearing before this court on an Order to Show Cause issued against the Bank of Marin and Eureka Fisheries, Inc., d/b/a Eureka Seafoods, on November 27, 1963, said hearing having been had before said court on December 20, 1963, Dinkelspiel & Dinkelspiel (Harold A. Block, Esquire) appearing as counsel for the applicant trustee herein, respondent Eureka Fisheries, Inc., d/b/a Eureka Seafoods, appearing through Messrs. Mathews & Traverse, and respondent Bank of Marin appearing through Messrs. Freitas, Allen, McCarthy & Bettini, and after hearing the allegations and proofs of the parties, the arguments and stipulations of counsel, and being fully advised in the premises, the following Findings of Fact and Conclusions of Law constituting the decision of the court in said matter are hereby made:

[fol. 58] Findings of Fact

1. That Marin Seafoods, Inc. filed its voluntary petition in bankruptcy in the United States District Court for the Northern District of California, Southern Division, on September 26, 1963;

[File endorsement omitted]

2. That John M. England was, by said court, duly appointed as receiver of said Marin Seafoods, Inc. on September 20, 1963, was qualified as such receiver, and did act as such receiver until October 20, 1963, at which time said John M. England became, and has been continuously, the duly elected, appointed, and qualified and acting trustee in bankruptcy of Marin Seafoods, Inc.;

3. That on the date of the filing of the aforesaid voluntary petition in bankruptcy herein, to wit on the 26th day on September, 1963, there was due and owing from customers of said Marin Seafoods, Inc., sums of money in excess of $3,200.00 for merchandise previously delivered by said Marin Seafoods, Inc. to said customers;

4. That without the knowledge or consent of the said receiver (later the trustee in bankruptcy herein), the said Marin Seafoods, Inc., through its principal officer, collected certain of its aforesaid accounts receivable (or portions thereof) and deposited said collections to the bank account of said Marin Seafoods, Inc. in a commercial bank account at the Bank of Marin to the account of "Marin Seafoods, Inc.," account No. 16-00139, on the date and in the amounts specified below, to wit:

Deposits	*Dates*
$604.30	September 27, 1963
251.51	September 27, 1963
503.72	September 27, 1963
892.04	September 30, 1963
588.45	October 2, 1963
207.35	October 3, 1963
66.80	October 4, 1963
67.92	October 8, 1963
TOTAL: $3,182.09	

[fol. 59] 5. That on the 3rd day of October, 1963, the Bank of Marin received from the said John M. England, the then receiver of the bankrupt corporation, a letter dated October 2, 1963, a true copy of which is attached as Exhibit "B" to the "Answer of Respondent Bank of Marin"; that said Bank of Marin on October 3, 1963 answered said letter, a true copy of which said answering letter is attached as Exhibit "C" to the aforesaid "Answer of Respondent Bank of Marin";

6. That during the period dating from September 27, 1963 and October 3, 1963 (both dates inclusive) the said Bank of Marin honored and paid certain checks drawn by the said Marin Seafoods, Inc. in favor of Eureka Seafoods as follows:

Check No.	*Date Drawn*	*Date Honored*	*Amount*
#675	Aug. 27, 1963	Oct. 2, 1963	$609.45
#705	Sept. 10, 1963	Oct. 2, 1963	630.42
#708	Sept. 13, 1963	Oct. 2, 1963	492.96
#712	Sept. 16, 1963	Oct. 2, 1963	141.68
#714	Sept. 17, 1963	Oct. 2, 1963	438.31
		TOTAL:	$2,312.82

7. That said checks, and each of them, were so honored and so paid without the knowledge or consent of the said John M. England as receiver herein; that the said Eureka Fisheries did thereby receive the aforesaid sum of $2,312.82;

8. That on October 14, 1963, said John M. England as receiver herein mailed to Bank of Marin a letter, a true copy of which is attached to the "Answer of Respondent Bank of Marin" as Exhibit "D"; that in response thereto, said Bank of Marin, under date of October 17, 1963, mailed to said John M. England as receiver herein a bank statement, a true copy of which is attached to "Answer of Respondent Bank of Marin" as Exhibit "A", together with its check in the sum of $168.80; that it was not until the 18th day of

October, 1963, that said John M. England as the receiver herein discovered the making of the deposits to the bank account described in Paragraph 4 hereof, and the honoring [fol. 60] and payment of the said checks described in Paragraph 6 hereof;

9. That at no time prior to October 3, 1963, did the Bank of Marin have any actual knowledge of the bankruptcy proceedings herein.

From the foregoing Findings of Fact, the court concludes:

Conclusions of Law:

1. This court has summary jurisdiction over Bank of Marin and Eureka Fisheries, Inc., d/b/a Eureka Seafoods;

2. That Marin Seafoods, Inc. was duly adjudged bankrupt on September 26, 1963;

3. That John M. England, the trustee herein, is entitled to judgment in the sum of $700.40 against the respondent Bank of Marin;

4. That the said John M. England, as trustee herein, is further entitled to judgment in the sum of $2,312.82 against the Bank of Marin and Eureka Fisheries, Inc., d/b/a Eureka Seafoods, jointly; and

5. The lack of actual knowledge of the Bank of Marin of the filing of the voluntary petition in bankruptcy by Marin Seafoods, Inc. accords the Bank of Marin no protection against the trustee's claims herein.

Let judgment be entered accordingly.

Dated this 31st day of March, 1964.

Lynn Gillard, Referee in Bankruptcy.

[fol. 61]

IN THE UNITED STATES DISTRICT COURT

FOR THE NORTHERN DISTRICT OF CALIFORNIA

SOUTHERN DIVISION

No. 74820

In Bankruptcy

[Title omitted]

JUDGMENT—March 31, 1964

Upon the Findings of Fact and Conclusions of Law this day entered in these proceedings, it is

Ordered, Adjudged and Decreed that John M. England, as trustee herein, have judgment against the Bank of Marin for the sum of $700.47; and it is further

Ordered, Adjudged and Decreed that John M. England have an additional judgment against the Bank of Marin and Eureka Fisheries, Inc., d/b/a Eureka Seafoods, jointly, for the sum of $2,312.82.

Dated this 31st day of March, 1964.

Lynn Gillard, Referee in Bankruptcy.

[File endorsement omitted]

[fol. 62]

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF CALIFORNIA
SOUTHERN DIVISION

No. 74820

In Bankruptcy

[Title omitted]

ORDER EXTENDING TIME TO FILE PETITION OF REVIEW—April 8, 1964

The Petition of the Bank of Marin for an extension of time to file a Petition for Review having been filed herein on April 8, 1964 and good cause appearing therefor:

It Is Hereby Ordered that the Bank of Marin be granted an extension of 20 days from April 10, 1964, in which to file a Petition for Review of the Order herein dated March 31, 1964.

Dated: This 8th day of April, 1964.

Lynn Gillard, Referee in Bankruptcy.

[File endorsement omitted]

[fol. 63]

IN THE UNITED STATES DISTRICT COURT

FOR THE NORTHERN DISTRICT OF CALIFORNIA

SOUTHERN DIVISION

No. 74820

In Bankruptcy

[Title omitted]

PETITION FOR REVIEW OF REFEREE'S ORDER—
Filed April 23, 1964

To: Lynn J. Gillard, Referee in Bankruptcy:

The Petition of the Bank of Marin respectfully represents:

1. Your petitioner is aggrieved by the Order herein of Lynn J. Gillard, Referee in Bankruptcy, dated March 31, 1964, a copy of which Order is annexed hereto, marked Exhibit "A" and made a part hereof.

2. The Referee erred in respect to said Order, in that the Referee's Conclusion of Law number 4, that John M. England, the Trustee herein, is entitled to judgment in the sum of $2,312.82 against the Bank of Marin and Eureka Fisheries, Inc., dba Eureka Seafoods, jointly, is contrary to the provisions of the Bankruptcy Act and the applicable law relating thereto in so far as it imposes liability upon the Bank of Marin.

3. The Referee erred in respect to said Order, in that the Referee's Conclusion of Law number 5, that the lack of actual knowledge of the Bank of Marin of the filing of the voluntary Petition in Bankruptcy by Marin Seafoods, Inc. accords the Bank of Marin no protection against the Trustee's claims herein, is contrary to the provisions of the Bankruptcy Act and the applicable law relating thereto

and deprives the Bank of Marin of property without due [fol. 64] process of law in violation of the United States Constitution Amendment No. 5.

4. That the Referee erred in respect to said Order, in that the Order, ordering, adjudging and decreeing that John M. England have a judgment against the Bank of Marin and Eureka Fisheries Inc. dba Eureka Seafoods, jointly, for the sum of $2,312.82, insofar as it relates to the Bank of Marin is contrary to the provisions of the Bankruptcy Act and the applicable law relating thereto.

Wherefore, your petitioner prays that said Order be reviewed by a Judge in accordance with the provisions of the Bankruptcy Act, that said Order be reversed, that the lack of actual knowledge of the Bank of Marin of the filing of the voluntary Petition in Bankruptcy of Marin Seafoods, Inc. be found to accord the Bank of Marin protection against the Trustee's claims herein, and that your petitioner have such other and further relief as is meet and proper in the premises.

Dated: April 22, 1964.

Bank of Marin, By Burton R. Kirchner, Vice President;

Freitas, Allen, McCarthy & Bettini, By Bryan R. McCarthy.

[File endorsement omitted]

[fol. 65]

IN THE UNITED STATES DISTRICT COURT

FOR THE NORTHERN DISTRICT OF CALIFORNIA

SOUTHERN DIVISION

No. 74820

In Bankruptcy

[Title omitted]

CERTIFICATE ON PETITION FOR REVIEW—
Filed April 27, 1964

The undersigned Referee in Bankruptcy hereby certifies that the record of the Court pertaining to the petition for review filed herein consists of the following:

1. Trustee's Application For Turnover Order, filed November 27, 1963;
2. Order To Show Cause, filed November 27, 1963;
3. Answer of Bank of Marin, filed December 16, 1963;
4. Answer of Eureka Fisheries, filed December 20, 1963;
5. Hearing on order to show cause held December 20, 1963;
6. Trustee's Memorandum, filed December 30, 1963;
7. Eureka Fisheries Memorandum, filed January 10, 1964;
8. Bank of Marin Memorandum, filed January 31, 1964;
9. Trustee's Reply Memorandum, filed February 14, 1964;
10. Opinion For Order, filed February 24, 1964;
11. Trustee's Proposed Findings, lodged February 27, 1964;

[File endorsement omitted]

[fol. 66] 12. Bank of Marin Proposed Findings, lodged March 2, 1964;

13. Hearing on settlement of findings, held March 18, 1964;

14. Findings and Conclusions, filed March 31, 1964;

15. Judgment, filed March 31, 1964;

16. Order Extending Time, filed April 8, 1964;

17. Petition For Review, filed April 23, 1964.

Question Presented

This petition for review is filed only by the Bank of Marin. The question presented is whether a bank is liable to the trustee in bankruptcy for the amount disbursed from the checking account of a bankrupt after an adjudication in bankruptcy, where the bank does not have actual notice of such bankruptcy.

Facts

Marin Seafoods, Inc. filed a voluntary petition in bankruptcy on September 26, 1963 and was adjudicated a bankrupt on the same day. Thereafter and between September 27, 1963 and October 8, 1963 Marin Seafoods, Inc. collected certain accounts receivable and deposited such collections in its checking account with the Bank of Marin. Of these deposits $168.80 was delivered by the bank to the trustee on October 17, 1963. After the date of adjudication in bankruptcy but prior to October 17, 1963, the Bank of Marin honored various checks drawn on the bank account totaling $700.40. In this petition for review the bank has not contested the order that it is liable to the trustee for this $700.40.

Additional checks drawn by the bankrupt totaling $2,312.82 drawn in favor of Eureka Fisheries were honored by the bank on October 2, 1963. These funds were paid by Bank of Marin without the knowledge or consent of the

trustee and were received by Eureka Fisheries. In paying these checks the Bank of Marin did not have any actual knowledge of these bankruptcy proceedings.

The Referee took the position that title to these funds [fol. 67] was at *all times* vested in the trustee and that both the bank, in divesting the trustee of possession, and Eureka Fisheries, the recipient thereof, were jointly liable to the trustee for repayment of the same.

Transmitted herewith are all of the documents hereinabove referred to, together with a transcript of the hearing on December 20, 1963.

Dated at San Francisco, California; April 27, 1964

Respectfully submitted,

Lynn Gillard, Referee in Bankruptcy.

[fol. 68]

IN THE UNITED STATES DISTRICT COURT

FOR THE NORTHERN DISTRICT OF CALIFORNIA

SOUTHERN DIVISION

No. 74820

In Bankruptcy

[Title omitted]

NOTICE OF PAYMENT AND CLAIM TO CONTRIBUTION—
Filed May 21, 1964

To: Lynn J. Gillard, Referee in Bankruptcy: to John M. England, Trustee, and His Attorneys, Dinkelspiel & Dinkelspiel: And to Bank of Marin and Its Attorneys, Freitas, Allen, McCarthy & Bettini:

Take notice that Eureka Fisheries Inc., a corporation, doing business as Eureka Seafoods, has paid the judgment

for $2312.82 in the above-entitled matter entered March 31, 1964, and does claim contribution from its joint judgment debtor, Bank of Marin.

Dated: May 19, 1964.

Mathews & Traverse, By Francis B. Mathews, Attorneys for Eureka Fisheries Inc., a corporation.

[File endorsement omitted]

[fol. 69] Affidavit of Service by Mail (omitted in printing).

[fol. 70]

IN THE UNITED STATES DISTRICT COURT

FOR THE NORTHERN DISTRICT OF CALIFORNIA

SOUTHERN DIVISION

No. 74820

In Bankruptcy

[Title omitted]

MEMORANDUM OF POINTS AND AUTHORITIES—
Filed June 15, 1964

I

Notwithstanding the provisions of Section 70a(5) of the Bankruptcy Act, a bank is not liable to the Trustee in Bankruptcy when, in good faith and without actual knowledge of the bankruptcy proceedings, it honors the bankrupt's checks in the regular course of its business after the adjudication of bankruptcy. *Rosenthal* v. *Guaranty Bank and Trust Co.* (D. C. La.) 139 F.Supp. 730; "Brady on Bank Checks", 3rd Ed. (1962) pp 2425, 313.

The *Rosenthal* case, supra, involved the same issue that is presented herein. The pertinent facts of that case are as

[File endorsement omitted]

follows: On October 3 the bankrupt filed a voluntary petition for corporate reorganization under Chapter X of the Bankruptcy Act in the Federal District Court in New York. The petition was approved by an Order of Court the same day. Approval of a Chapter X petition is equivalent to an adjudication of bankruptcy for the purpose of applying the provisions of Chapters I through VII of the Bankruptcy Act. (Bankruptcy Act Section 102). Subsequently, from October 4 to October 10 the defendant, in Louisiana Bank, honored checks amounting to approximately $7,000.00, drawn upon the bank by the bankrupt prior to the filing of the petition. The Court found as a fact that the bank had [fol. 71] no "actual knowledge" of the bankruptcy proceeding until formal notice was received from the Trustee on October 11. The Trustee then brought suit against the bank to recover the sum of $7,000.00. The Court held that there was no liability on the part of the bank.

The Court in the *Rosenthal* case, supra, relied upon Bankruptcy Act Section 70d(5) for its holding that the bank was protected. That section provides as follows:

> "A person asserting the validity of a transfer under this subdivision shall have the burden of proof. Except as otherwise provided in this subdivision and in subdivision (g) of section 44 of this title, no transfer by or in behalf of the bankrupt after the date of bankruptcy shall be valid against the Trustee; *provided, however, that nothing in this title shall impair the negotiability of currency or negotiable instruments.*" (Emphasis added)

The Court stated that one of the purposes of the negotiability clause as it appears in the above cited section of the Bankruptcy Act is to protect a bank who in good faith, for present equivalent value, in the ordinary course of its business and without actual knowledge of the bankruptcy, honors checks drawn upon it by the bankrupt. *Rosenthal* v. *Guaranty Bank and Trust Co.*, supra, at page 736. To impose liability upon the bank would impair the nego-

tiability of a negotiable instrument. *Rosenthal* v. *Guaranty Bank and Trust Co.*, supra, at p. 734.

The policy governing the holding of the *Rosenthal* case, supra, and which is applicable herein, has been set forth frequently in earlier cases. (See cases infra: *Citizens National Bank* v. *Johnson* (6th Cir. 1923) 286 Fed. 527; *Matter of Retail Stores Delivery Corp.* (D. C. N. Y.) 11 F.Supp. 658). Although these decisions were decided prior to the 1959 amendment to Bankruptcy Act Section 18 (g) (now section 18 (f)) which was altered to provide that the filing of a voluntary petition constituted an automatic adjudication of bankruptcy, their reasoning is applicable here. Furthermore, it is questionable whether present Section 18 (f) would require a different conclusion in view of the doctrine of relation back that was then applicable. (See: Citizens National Bank v. Johnson (6th Cir. 1923) 286 Fed. 527). These earlier cases uniformly held that the bank, after the filing of a petition in bankruptcy, without actual notice of the filing of the petition, may, prior to adjudica-[fol. 72] tion, make payment to third persons upon the bankrupt depositor's checks without incurring liability to the Trustee in Bankruptcy. *Citizens National Bank* v. *Johnson* (6th Cir. 1923) 286 Fed. 527; *Matter of Retail Stores Delivery Corp.* (D. C. N. Y.) 11 F.Supp. 658; *Matter of Zotti* (6th Cir.) 186 Fed. 84, cert. denied 223 U.S. 718, 32 S. Ct. 522, 56 L. Ed. 628.

The reasoning behind these cases is set forth in the following quotations:

> "Most of these cases base the denial of a turnover order upon the grounds that the bank in question was unaware that a petition in bankruptcy has been filed, and it was held that under such circumstances it would be inequitable and impractical to make the bank refund to the Trustee the amount of such checks paid by it; otherwise, a bank could never pay a check without first ascertaining whether a petition in bankruptcy had been filed against the one who drew the check." (*Matter of*

Retail Stores Delivery Corp. (D. C. N. Y.) 11 F.Supp. 658, at 659)

"Its effect would be that the bank could not protect itself against liability to a trustee in bankruptcy subsequently appointed on account of payments made in good faith and in the regular course of business and in ignorance of the bankruptcy proceedings . . . except through the impossible course of keeping itself advised, not only daily, but momentarily, of the filing of petitions for adjudication of bankruptcy against its depositors in any competent jurisdiction. . . . True, broadly speaking, the adjudication when made relates back to the commencement of the bankruptcy proceedings for the purpose of adjudicating rights in equity generally. But we think that both on principle and authority the rule referred to does not make the banks liable for good faith payments to third persons made before adjudication upon depositors' checks in the regular course of business and without knowledge or notice of bankruptcy." *Citizens National Bank* v. *Johnson* (C.C.A. 6th Cir.) 286 Fed. 527.

The statements in the two above cited cases relating to the inequity and impracticability of holding a bank liable for honoring checks that were properly drawn on a bankrupt's account when the bank had no knowledge of the bankruptcy proceeding are equally as applicable to checks that were honored after adjudication as to checks that were honored before adjudication.

It is apparent that the Bank of Marin, which after adjudication, honored checks drawn by the bankrupt prior to the filing of the voluntary petition in bankruptcy, and did so in good faith without actual notice of the bankruptcy proceeding and in the ordinary course of its business, is not liable to the Trustee herein. *Rosenthal* v. *Guaranty Bank and Trust Co.*, supra.

[fol. 73] The decision of the Referee herein is not supported by authority. The Referee relies upon *Feldman* v. *Capitol Pierce Dye Works, Inc.* (C.A. 2d 1961) 293 F. 2d 889, which case is not in point. The *Feldman* case, supra, involved a situation where an officer of the corporate bankrupt, two days before the filing of an involuntary petition, transferred the bankrupt's account to an account in his own name for the purpose of paying the bankrupt's payroll. The Court found that the circumstances surrounding such transfer were such that it did not divest the bankrupt of ownership of the funds, but merely constituted a change of name in the account. The Court further found that the officer had resigned on the same day and that therefore he had no actual authority to sign the checks payable from the account. The Court held that the bank was liable to the Trustee in Bankruptcy for checks drawn by the resigned officer and paid by the bank upon the officer's individual and personal authorization after the filing of the petition, notwithstanding the fact that the bank had no knowledge of the pending bankruptcy. The holding was based upon the bank's reliance on the resigned officer's oral representations that he had authority to transfer the account and to write the checks. As a result it could not be said that the bankrupt's indebtedness, represented by checks, was paid upon the bankrupt's order as required in Bankruptcy Act Section 70d (2). Furthermore, Bankruptcy Act 70d (5) was not applicable because the checks were not negotiable instruments as they lacked the signature of an authorized officer. The Court did not state that section 70d (5) was inapplicable because there was no impairment of the negotiability of a negotiable instrument.

II

Except as to matters governed by the Federal Constitution or Federal Statutes, State law is to be applied. This includes State statutory as well as decisional law. *Erie Railroad Co.* v. *Tompkins* 304 U.S. 64, 58 S. Ct. 817, 82 L. Ed. 1188. It is well settled that the existence of all

claims, liens and equities in bankruptcy proceedings are to be determined, in the absence of Federal Statutes, by the applicable State law. *Porter* v. *Searle* (C.A. 10th 1955) 228 F. 2d 748; *Commercial Credit Co.* v. *Davidson* (C.A. [fol. 74] 5th 1948) 112 F. 2d 59. And as to matters which are not provided for by the Bankruptcy Act, State law remains operative. *Stellwagen* v. *Clum* 245 U.S. 605, 62 L. Ed. 507, 38 S. Ct. 215.

There is no provision in the Bankruptcy Act providing for the type of notice that must be given to a bank where the bankrupt has deposits. Nor are there any provisions providing for the type of notice that must be given to a debtor of the bankrupt. (Note: that the relationship between the depositor and the bank is one of creditor and debtor. See: *In re Retail Stores Delivery Corp.* (D.C.N.Y. 1935) 11 F.Supp. 658.) Consequently State law providing for such notice will be applied.

In this regard California Financial Code Section 952 provides in part as follows:

> "Notice to any bank of an adverse claim (the person making such an adverse claim being hereinafter in this section called 'adverse claimant') to a deposit standing on its books to the credit of or to personal property held for the account of any person may be disregarded until and unless the adverse claimant shall (a) procure and serve upon the bank at the office at which the deposit is carried or the property held a restraining order, injunction, or other appropriate order against the bank from a court of competent jurisdiction in an action in which the adverse claimant and all persons in whose name such credit stands or for whose account such property is held are parties; . . ."
>
> "*Unless such restraining order, injunction, or other appropriate order is obtained . . . the bank,* notwithstanding such notice, *may honor the checks* . . . requiring the payment of money *by or for the account of the person to whose credit the account stands or may deliver*

such property to, or on the order of the person for whose account such property is held, without any liability on the part of the bank . . . " (Emphasis added).

The purpose of enacting Financial Code Section 952 was to avoid placing banks in the dilemma that arises when a check drawn by the depositor upon his account with the bank is presented for payment and a third party also claims to have an interest in the account. The bank is thus placed in the position of incurring liability to either the depositor if it fails to honor the check or to the third party if it honors the check and the third party's claim proves to be valid. (See: *Gendler* v. *Sibley State Bank* (N.D. Iowa 1945) 62 F.Supp. 805). This is exactly the problem which is presented here.

A similar Statute was dealt with in *First National Bank* [fol. 75] *of Arizona* v. *Butler* 82 Ariz. 361, 313 P.2d 421 (1957) wherein the Court stated that the Trustee in Bankruptcy would be governed by the Statute if he were an "adverse claimant". However, the Court in *First National Bank of Arizona* v. *Butler,* supra, held that the Trustee could not be an "adverse claimant" under the facts therein. The bankrupt consisted of a partnership. The bank transferred the bank account to the spouse of a deceased partner. The Court stated that the Trustee was not an "adverse claimant" because he stood in the shoes of all bankrupt partners, including the deceased partner.

The situation herein is distinguishable. The relationship of the depositor and the bank is that of a debtor and creditor. In re *Retail Stores Delivery Corp.* (D.C.N.Y. 1935) 11 F.Supp. 658. A Trustee seeking to recover bank deposits of a bankrupt which are claimed by a payee of a check issued by the bankrupt after the petition had been filed against him is an "adverse claimant". In re *Fuller* (C.C.A. 2nd Cir. 1923) 294 Fed. 71. Consequently, the Trustee in Bankruptcy may not hold the bank liable under the facts herein as the Trustee is an "adverse claimant" and as such failed to give the bank notice required by California Financial Code Section 952.

III

Not only is the position of the Trustee and Referee herein contrary to existing authority, but it is unreasonable, impractical and inequitable. The decision of the Referee places upon the bank the impossible task of ascertaining whether or not a depositor has filed a petition in bankruptcy before it honors the checks drawn by the depositor. As pointed out previously (see *Matter of Retail Stores Delivery Corp.*, supra; and *Citizens National Bank* v. *Johnson*, supra), this requires that the bank keep itself advised momentarily of the filing of a petition in bankruptcy by its depositors. The impossibility of this task is further magnified by the fact that the filing of a petition in any District Court within the United States would affect the bankrupt's bank deposits located in any jurisdiction. (See *Citizens National Bank* v. *Johnson*, supra).

Furthermore, even if it were possible for the bank to keep itself so advised, the bank is not able to delay the honoring of a check until it ascertains whether or not the depositor has filed a petition in bankruptcy. A bank is [fol. 76] under a legal obligation to honor checks drawn upon it, when presented in proper form and correctly endorsed, as long as there are funds on deposit to the credit of the depositor sufficient in amount to pay the checks. And if the bank refuses to pay a check drawn by a depositor which fulfills these conditions, it may become liable to the depositor in damages. *Weaver* v. *Bank of America* 59 Cal. 2d 432 (1963); *Reeves* v. *First National Bank* 20 C.A. 508 (1912); *Allen* v. *Bank of America* 58 C.A. 2d 124 (1943).

The bank, by reason of the decision of the Referee, is placed in a position where it will incur liability to the Trustee if it honors a check properly drawn by a depositor which is presented for payment after the filing of a voluntary petition even if the bank has no actual knowledge of such a filing. On the other hand, a bank will incur liability to the depositor if it fails to honor a check properly drawn upon sufficient funds. The bank as a result is placed in a position of incurring liability no matter what course it

decides to follow. To say that the bank would not incur liability to the depositor if it fails to honor his check promptly because the depositor had in fact filed a voluntary petition in bankruptcy does not resolve this dilemma. This would be to view the problem in restropect, an advantage the bank does not have at the time the check is presented for payment.

A Bankruptcy Court is a Court of equity. *Pepper* v. *Litton* 308 U.S. 295, 60 S. Ct. 238, 84 L. Ed. 281. As such, it is obligated to exercise broad equitable powers. *Pepper* v. *Litton,* supra; *New York Terminal Warehouse Co.* v. *Bullington* (C.C.A. 5th) 213 F. 2d 340. It is a travesty upon those powers to impose liability upon the bank in the situation that has been presented herein. The only reasonable, practical and equitable result, as well as the only result that is supported by authority, would be not to impose liability upon a bank which honors checks in the regular course of its business which checks were drawn prior to the filing of a voluntary petition in bankruptcy but presented afterwards, where the bank has no actual knowledge of the bankruptcy proceedings.

IV

Moreover, the Trustee herein is estopped to assert his [fol. 77] claim against the bank. The defense of equitable estoppel is proper as the Bankruptcy Court is a Court of equity. *Pepper* v. *Litton,* supra. An equitable estoppel arises where one does something he should not have done, or fails to do something he should have done, if the person invoking the doctrine was prejudiced by the party to be estopped. *Brown-Crunner Investment Co.* v. *Poulter* 70 F. 2d 184; *Union Mutual Insurance Co.* v. *Wilkinson* 80 U.S. 222, 13 Wall 222, 20 L. Ed. 617; *Banco Mercantile* v. *Sauls Inc.* 140 C.A. 2d 316 (1956); *DeHamanti* v. *Lompoc Union School Dist.* 143 C.A. 2d 715 (1956).

The Trustee herein, had he given timely notice to the bank, could have avoided the entire problem. However, although the voluntary petition was filed on September 26, 1963, the first notice given to the bank of the pending bank-

ruptcy proceeding was received by the bank on October 3, 1963. The checks that were honored by the bank and which are the subject of this dispute were so honored on October 2, 1963. The Trustee (formerly the Receiver) knew from the schedules of the bankrupt herein that the bankrupt had an account at the Bank of Marin. Furthermore, the Trustee as a reasonable man must have known that it was very possible that the bankrupt had drawn checks on that account prior to the filing of the voluntary petition and that some of said checks would be presented for payment after the filing of the petition. Yet the Trustee failed to notify the bank of the bankruptcy proceedings. The failure of the Trustee to speak under the circumstances herein misled the bank into taking action to its detriment. The requirements necessary for the imposition of the Doctrine of Equitable Estoppel are present. Consequently, the Doctrine of Equitable Estoppel may be raised as a defense by the bank and as such constitutes a defense against the claim of the Trustee.

V

If the ruling of the Referee is permitted to stand, a serious constitutional issue is raised. By interpreting sections 18 (f) and 70 (a) of the Bankruptcy Act in a manner so as to impose liability upon the bank under the facts herein, the bank is being deprived of its property without due process of law in violation of the United States Constitution Amendment V. The bank, faced with a legal obligation to honor a check that is properly drawn upon sufficient [fol. 78] funds, will incur liability if it does not honor such a check. *Weaver* v. *Bank of America* 59 Cal. 2d 432 (1963). As a result, when a properly drawn check is presented for payment, the bank must honor it if the drawer has sufficient funds on deposit. However, by fulfilling this legal obligation, the bank incurs liability to the Trustee in Bankruptcy of the bankrupt depositor who has filed a voluntary petition in bankruptcy, the bank having no actual knowledge or notice of the bankruptcy proceedings. This is a taking of the bank's property without due process of law.

The due process clause of the Fifth Amendment is applicable to the Bankruptcy Act and bankruptcy proceedings. *Louisville Joint Stock Land Bank* v. *Radford* 295 U.S. 555, 55 S. Ct. 854, 79 L. Ed. 1593; *Wright* v. *Vinton Branch of Mountain Trust Bank* 300 U.S. 440, 57 S. Ct. 556, 81 L. Ed. 736; *In re Burke* 51 F. Supp. 552 (1943). Furthermore, corporations are persons within the meaning of the constitutional provision forbidding the deprivation of property without due process of law as required by the Fifth Amendment. *Union Pacific Railroad Co.* v. *United States* 99 U.S. 700, 25 L. Ed. 496.

Generally speaking, bankruptcy proceedings are in the nature of proceedings in rem and as such it is necessary that interested parties be given notice of the proceedings as is required in proceedings in rem. *Hanover National Bank* v. *Moyses,* 186 U. S. 181, 22 S. Ct. 857 (1902), 46 L. Ed. 1113. Due process requires that such notice be reasonably calculated, under all the circumstances, to apprise interested parties of the pendency of the action. *Mullane* v. *Central Hanover Bank and Trust Co.,* 7 U.S. Ct. 652, 339 U.S. 306, 94 L. Ed. 865 (1949).

By no means can it be considered that the mere filing of a voluntary petition in bankruptcy is notice reasonably calculated to put the bank on notice of the pending proceedings so that it may avoid incurring liability to the Trustee. It is submitted that reasonable notice under the circumstances would be notice mailed to the bank advising it of the bankruptcy proceedings. This would require a minimal effort on the part of the Bankruptcy Court or Trustee and would be sufficient to put the bank on notice so that it may protect itself.

[fol. 79] By way of analogy the *Hanover National Bank* v. *Moyses* case, supra, is relevant. The Court in that case held that the notice given a creditor of the bankrupt of the pending proceedings was sufficient to give him notice of the proceedings and of the discharge of the bankrupt and consequently, the Bankruptcy Act did not violate the due process clause of the Fifth Amendment in this regard. The Court rested its holding on the fact that the bankrupt is

required to list his creditors in his schedule and that if the creditor is not so listed, the creditor has a basis for preventing the bankrupt's obligation to him from being discharged. As to the creditors listed in the schedules, they must be given at least ten days notice by publication and by mail of the first meeting of creditors and of each of the various subsequent steps in administration. (Bankruptcy Act Section 58). An application for discharge could not be made until at least one month after adjudication (Bankruptcy Act Section 14). Notice of the hearing for discharge must then be given by publication and mail (Bankruptcy Act Section 14 and Section 58). The Court stated that the notice provided for in the Bankruptcy Act, as outlined above, was sufficient to put a creditor on notice of the proceedings and of the discharge of the bankrupt.

No such notice was given to the bank herein before its property was taken. A creditor only loses a property right upon the bankrupt's discharge (Bankruptcy Act Section 17) and of this he has sufficient notice. The bank loses a property right upon honoring a check properly drawn in the ordinary course of business even though it has no notice of the bankruptcy proceedings. It is apparent that the mere filing of a voluntary petition in bankruptcy falls short of the notice that has been held to be sufficient in the *Hanover* case, supra.

Dated: This 15 day of June, 1964.

Respectfully submitted,

Freitas, Allen, McCarthy & Bettini, Attorneys for Petitioner, Bank of Marin.

[fol. 80]

IN THE UNITED STATES DISTRICT COURT

FOR THE NORTHERN DISTRICT OF CALIFORNIA

SOUTHERN DIVISION

No. 74820

In Bankruptcy

TRUSTEE'S MEMORANDUM OF POINTS AND AUTHORITIES —Filed August 17, 1964

I

The basic question involved in appellant's Petition for Review, to wit, whether or not a bank which, subsequent to the filing of a *voluntary* petition in bankruptcy by its depositor, honors the checks of its aforesaid depositor prior to receiving *actual* notice of such bankruptcy, is liable to the trustee therefor, is of such tremendous importance, not only to the Bankruptcy Bar, but to the business of banking, that, prior to answering the Appellant's Memorandum of Points and Authorities herein, we feel it our obligation to advise the court that a collateral and serious question has arisen in this case, not appearing on the record, which might make the principal problem moot. The facts giving rise to the collateral problem are as follows:

An examination of the record before the court will indicate that the referee herein granted a *single* judgment against the Bank of Marin and in favor of the trustee for $700.47, and a *joint* judgment against Eureka Fisheries [fol. 81] *and* the Bank of Marin and in favor of the trustee for the further sum of $2,312.82. The Bank of Marin did not appeal from the *single* judgment against it in the sum of $700.47, and, as a matter of fact, has already paid the same to the trustee.

[File endorsement omitted]

The Bank did, however, appeal from the *joint* judgment awarding the sum of $2,312.82 in favor of the trustee and against the Bank *and* Eureka Fisheries. Eureka Fisheries, however, did *not* appeal from the aforesaid joint judgment, and, as a matter of fact, on or about May 19, 1964, paid the entire amount ($2,312.82) to the trustee. In so doing, however, Eureka Fisheries did, in fact, file in the bankruptcy proceeding a document entitled "Notice of Payment and Claim to Contribution", a true copy of which is attached hereto, and marked Exhibit "A".

We are not attempting herein to pass upon the legal effect (if any) of said Notice of Payment and Claim to Contribution. We recognize, of course, the possibility that Eureka Fisheries might at some time in the future institute a civil action against the Bank of Marin claiming a right to be reimbursed by the Bank of Marin for one-half of this payment ($1,156.41). (*California Civil Code*, Sec. 1432.)

The trustee in this case, therefore, finds himself in the rather favored position of having already recovered in full his entire initial demand; he cannot be required by either the Bank of Marin or Eureka Fisheries to return this money no matter how the present Petition for Review is decided by this court.

With respect to the joint judgment we are informed, and verily believe, that the Bank had no knowledge whatsoever of the payment by Eureka Fisheries of the joint judgment to the trustee until the "Notice of Payment and Claim to Contribution" was filed in the Bankruptcy Court.

We further assume, that should this court reverse the joint judgment for $2,312.82 *against the Bank of Marin*, [fol. 82] it would have no jurisdiction to reverse it as against Eureka Fisheries, since Eureka Fisheries has not appealed therefrom. In other words, from a strictly monetary point of view, the trustee has no interest whatsoever in the present Petition for Review filed by the Bank of Marin. So far as the trustee is *monetarily* concerned, the

problem is moot. It is also presently moot as against the Bank of Marin since the Bank has parted with nothing. There is simply no jurisdiction in this court to order the trustee to return to the non-appealing party (Eureka Fisheries) the money which it voluntarily paid to the trustee in satisfaction of Eureka Fisheries' joint liability to the trustee.

With respect to this particular problem, so far as the Bank of Marin is concerned, however, we recognize a considerable difference in effect. Should the Bank not be in a position to question the validity of the referee's joint judgment, it might be forced to meet the issue of *res adjudicata* in subsequent possible litigation between the Eureka Fisheries and the Bank regarding the liability of a joint judgment debtor for contribution. In other words, if Eureka Fisheries brings suit for contribution against the Bank, it (Eureka Fisheries) could well take the position that it has already been decided by a valid court judgment that the obligation was joint, and that consequently Eureka's right to contribution from the Bank cannot be further questioned. Consequently, it is our belief that the issue is not moot in the *legal* sense.

Whether or not a particular issue between litigants is *res adjudicata* is, of course, a matter of substantive law, and therefore governed by the state law. A research of the California law has produced two relevant cases:

In *Estate of Merrill,* 29 Cal. 2nd 520, 175 P.2d 819 (1946), a joint judgment against a special administrator and his attorney was satisfied by the administrator without the [fol. 83] attorney's consent. The court said:

> "There was no voluntary satisfaction of the judgment by McMahon, the party seeking to proceed with the appeal, but rather the judgment was paid by his joint obligor, without McMahon's knowledge or consent. Under these circumstances showing that the judgment was satisfied without the acquiescence of McMahon, Section 1049 of the Code of Civil Procedure cannot be invoked to impair or destroy his right of appeal . . .

"If McMahon is not allowed to proceed with his appeal, the judgment in question would attain finality as to these issues without his having the opportunity to test before an appellate court the merits of their adjudication adverse to him." 29 C.2nd, at 524-5.

Similarly here, if the Bank's appeal is held to be moot, we would preclude the Bank from ever testing in an appellate court the trustee's right to recover under the circumstances present in this case.

In *Metcalf* v. *Drew,* 75 C.A. (2nd) 711, 171 Pac. (2d) 488 (1946), the court (in citing a Texas case) said:

"Ordinarily, in such cases, it would be sufficient to dismiss the appeal. To do so in this case, however, would leave the judgment appealed from intact so that it could be pleaded in future as *res adjudicata* . . .

"In the instant case, we are not confronted with the voluntary satisfaction of the judgment in the Superior Court, but a case wherein, without either the consent or knowledge of appellant Charlesworth, the judgment was satisfied by the [co-respondent] . . . Notwithstanding the satisfaction of the judgment by the [co-respondent] . . . we hold that the question raised on this appeal cannot be considered as entirely moot . . . the appeal should be determined on its merits." 75 C.A. 2nd at 721-2. See also *Hartke* v. *Abbott,* 106 Cal. App. 388, 289, p. 206.

We are most aware of the natural reluctance on the part of an appellate court to pass upon moot problems. We believe the problem presented here, however, although *monetarily* moot to the trustee, is clearly not moot with [fol. 84] respect to the substantive rights of the Bank of Marin and Eureka Fisheries regarding Eureka Fisheries' possible claim to contribution from its joint judgment debtor. Again, we state that the basic question herein in-

volved is of such importance that the onerous burden of determining the answer to it should not lightly be imposed upon an appellate court without informing that court that the trustee herein has no monetary interest in this present appeal. The trustee's interest is, accordingly, only academic. If this court, therefore, determines that the issue is moot, it should not undertake to settle the important basic question hereinafter discussed.

In passing, we might add that should the court so desire, we have no objection to an order being made by this court deleting that portion of the joint judgment which imposes a liability on the Bank to the trustee for $2,312.82. We do this *solely* because the trustee has already effected a complete recovery and can be expected to accomplish nothing by defending against the Bank's appeal. Our offer should NOT be interpreted in ANY way as a retreat from the legal position we have taken in this case that a Bank is liable to a trustee in bankruptcy for cashing the checks of a bank's bankrupt depositor subsequent to the filing of such depositor's voluntary petition in bankruptcy despite the bank's lack of *actual* knowledge of the filing of such voluntary petition. On the other hand, if the court concludes that the basic question must be answered in this particular proceeding, we now proceed to answer the brief of the appellant.

II

The basic and important proposition that a bank which honors the checks of a *voluntary* bankrupt depositor drawn prior to the filing of the petition is liable to the trustee therefor despite lack of *actual* notice of such bank-[fol. 85] ruptcy proceedings on the part of the bank is fairly well covered in the Memorandums supplied by the trustee and opposing counsel to the Referee in Bankruptcy. We respectfully urge this court to examine those briefs carefully.

From an examination of Section I of the appellant's Memorandum of Points and Authorities herein, this court

will notice that appellant's entire line of reasoning is based primarily upon the case of *Rosenthal* v. *Guaranty Bank and Trust Company*. The most important thing to notice about the *Rosenthal* case is the fact that it was decided in 1956, approximately three years prior to the enactment of Section 18(f) of the Bankruptcy Act which made the filing of a voluntary petition in bankruptcy an automatic adjudication. No longer is there any time lag between the filing date and the date of adjudication in *voluntary* cases. Without the existence of such a time lag, therefore, Section 70(d) of the Bankruptcy Act by its express terms cannot and does not apply. Section 70(d), however, is the *only* section of the Bankruptcy Act that accords protection to any payments made from funds of the bankrupt subsequent to the filing date. The doctrine of relation back simply has no application whatsoever to the protection accorded by Section 70(d) of the Bankruptcy Act. That section clearly states that such a doctrine is not applicable where there is an hiatus between the date of the filing of the petition and the adjudication, during which time certain good faith payments are made from the bankrupt's funds. Actually, in the *Rosenthal* case, the Louisiana Company (Le-Blanc Corporation) filed a voluntary Chapter X proceeding under date of October 3, 1951. It was not until two and one-half years later that there was entered on June 7, 1954, an order adjudging the corporation bankrupt. In *Rosenthal*, therefore, there was an extended hiatus period. Although the payments that were made by the [fol. 86] bank there were made shortly after the filing of the petition (payments being made between October 4th and October 10th), a proper application of the facts of that case would clearly show that unless and until the bank received some sort of notice with respect to the existence of a bankruptcy proceeding, the bank should be (and accordingly was) protected. In other words, the court in the *Rosenthal* case was dealing with a completely different state of facts than we have here. In *Rosenthal*, the debtor

was continuing in business pursuant to the provisions of Chapter X. Clearly, under such circumstances and within the limitations provided by Section 70(d), the bank should be protected until it had notice of *actual* bankruptcy. In a *straight* bankruptcy situation, (under Chapters I-VII), such as we have in our case, however, no protection is accorded following the date of adjudication (the same date as the filing).

The reference of appellant's counsel herein to Sec. 102 of the Bankruptcy Act wherein the judicial act of approval of a Chapter X filing is deemed to be tantamount to an adjudication thereby making the *Rosenthal* case comparable to a regular voluntary bankruptcy proceeding where the adjudication is automatic makes no sense whatsoever. Obviously, the judicial act of approval of a Chapter X petition (see Secs. 112-116, inclusive) is NOT an adjudication in the sense that the debtor is thereupon adjudicated bankrupt. Quite to the contrary, it is a preliminary judicial blessing indicating to creditors and other parties in interest that, at least, the affairs of the debtor are not on the face of things so completely hopeless that bankruptcy adjudication is essential.

On the other hand, however, the *voluntary* filing of a straight bankruptcy petition is clearly an indication of that state of financial collapse wherein it is essential that adjudication follow immediately.

[fol. 87] Even in the *Rosenthal* case, the court recognized the philosophic differences of a conflict between the bankruptcy law and the law of negotiable instruments. District Judge Hunter highlights this conflict in the following language (page 734):

> "When the bankruptcy occurs the bank upon which the bankrupt drew a check prior to the date of the bankruptcy finds himself caught in the intermeshing of two highly complicated systems of law. Traditionally, it is the primary function of the Bankruptcy Act to pro-

tect the creditors, to marshal the assets, and to distribute them among the creditors equitably and ratably in accordance with their respective rights and interests. Negotiability tries to give the bank the maximum assurance that it will be able to cash the check without any defenses being interposed. An expansion of bankruptcy in some senses indisputably hinders the flow of commercial paper." 139 Fed. Supp. 734.

Collier criticizes the *Rosenthal* case in the following language:

"A good deal more is read into the proviso of clause five of the court in *Rosenthal* v. *Guaranty Bank & Trust Company* than was intended by the draftsman . . . [The court's] emphasis on the bank's good faith seems misplaced; good faith is relevant under Section 70 (d)(2), but that clause applies only to transactions *anterior* to adjudication . . . (emphasis supplied)

"To charge a depository bank with liability for cashing checks of its depositor after his adjudication does not impair the negotiability of the checks. Delivery of a check to the drawee bank for payment is not negotiation." 4 *Collier on Bankruptcy,* 1502.

A great deal has been said in the appellant's brief about the injustice and impracticability of a rule that the bank is not protected on payments made by it of funds belonging to the bankrupt's estate subsequent to bankruptcy where it has no actual notice of bankruptcy. The appellant has conjured up a picture of every bank having posted at the United States District Clerk's office some employee whose duty it shall be to advise the bank that a voluntary peti- [fol. 88] tion in bankruptcy has been filed by one its depositors, so as to obviate the possibility that checks drawn by such depositor might be inadvertently cashed by the bank subsequent to the bankruptcy. We note that the case

cited by the appellant on page 3 of their brief (*Citizens National Bank* v. *Johnson*) was decided approximately forty years ago (1923). In graphically pointing out the "impossible course of keeping itself advised, not only daily, but momentarily, of the filing of a petition for adjudication of bankruptcy against its depositors in any competent jurisdiction" it did state that the so-called "lack of notice rule" should apply only "*before* adjudication".

In order to properly understand this problem, therefore, it behooves us to examine carefully into the historical basis of protected transactions in bankruptcy. The most excellent historical analysis of the evolution of Section 70(d) of the Bankruptcy Act is, perhaps, contained in Volume 4, *Collier on Bankruptcy,* Section 70.66 and 70.67 (pages 1494-1501, inclusive).

> "Prior to the enactment of Section 70(d) as a part of the 1938 Act, there was no statutory law with respect to protected transactions in bankruptcy. Judge-made law, compelled by considerations of justice and equity, frequently moved to protect those whose bona fides in dealing with the bankrupt after bankruptcy were clear. But, as demonstrated hereafter, the situation was fraught with an uncertainty which might have delighted a disciple of the functionalist school of legal philosophy, but which held only the Damocles sword of possible economic loss suspended over those engaged in ordinary commercial pursuits. *The Act of 1938 brought an end to this, and the definitive standards of Section 70d supplanted the nebulous vagaries of the prior law.* The statutory innovation thus introduced was largely the result of the impetus furnished by one man—Professor James A. McLaughlin of Harvard University, whose article in the Harvard Law Review in 1927 urged some provision for protected transactions along the lines of the English Act. As there stated by Professor McLaughlin and later repeated by him in the *Analysis of H. R. 12889,* the situation was 'conducive to confusion

and uncertainty, with potentialities for argument, [fol. 89] "bluffing", litigation, expense, and delay.'

. . .

"As previously stated in the treatise, the courts prior to 1938 were faced with two contradictory concepts. On the one hand, despite the inconsistent language of Section 70a and the lack of definite statement in other provisions of the Act, the filing of the petition was held to be a *caveat* to the whole world, and in effect an attachment and injunction. This proposition was an essential prop to the bankruptcy court's assertion of jurisdiction and power in preventing the dissipation and attachment of the assets of the estate, in determining the rights of claimants under the various provisions of the Act, in fixing the right of set-off against the estate, in enjoining non-bankruptcy proceedings that interfered with the bankruptcy administration, and generally in adjudicating the very nature and extent of the bankruptcy court's exclusive control. On the other hand, the courts were often impelled to make exceptions to the doctrine where its application would work a hardship on an innocent party who, following the inception of bankruptcy, dealt with the bankrupt on a bona fide basis for a present consideration. The concept that the filing of the petition was a sort of *lis pendens* was probably justifiable and proper in the instances just previously enumerated, but where innocent parties were concerned, it was recognized that as a practical matter the mere filing of the petition gave rise to no actual notice that would put such persons on guard. *These propositions, of course were inherently inconsistent, and whether the one or the other would prevail in a close case was always a matter of conjecture.* Nor was the confusion improved by the gradual and parallel evolvement of the 'relation back' doctrine, which served to rationalize the introductory portion of Section 70a with the provisions of Section 70a(5)

and fixed the date of filing the petition as the date of cleavage with respect to the trustee's title. As a matter of fact, the former statement in the introductory portion of Section 70a that appeared to fix the trustee's title as of the date of adjudication was seized upon by some courts to justify the protection of a particular transaction, even though in other situations the time of filing came to be regarded as the determinative date.

"From this development, however, certain instances could be singled out where it was possible to predict [fol. 90] that the transaction, even if effected after bankruptcy, would be protected from invalidation. Thus it was held that an alleged bankrupt, acting in good faith, was entitled to conduct his business, enter into legitimate contracts in connection therewith and utilize his funds in paying the expenses of operation prior to his adjudication or until such time as a custodian or receiver was appointed to take charge of the estate. Payments of funds of the bankrupt, without notice of bankruptcy and in the usual course of business —as by a bank or an insurance company—, were also protected *prior to adjudication* or the appointment of some officer to have preliminary custody or possession of the estate. Of course, if the transactions were actually fraudulent or amounted to a preference of a creditor, whether the creditor was innocent or not, it could not be sustained. *And it was undisputed that after an adjudiction, in bankruptcy, all transfers of the bankrupt's property both by or to innocent parties were nonetheless invalid.* It was said that an adjudication was notice to all the world.

"Yet despite these instances, there remained considerable uncertainty as to how far and when the theory of protected transactions could be implemented. The courts themselves were cautious and somewhat doubtful in their language, and as Professor McLaughlin so

aptly pointed out, the situation was fraught with undesirable possibilities that demanded correction . . .

"It was admitted by the proponents of Section 70d that its enactment as a part of the 1938 Act would not tend to increase subsequent dividends to creditors of bankrupt estates. But, as pointed out by Professor McLaughlin, it was possible to go too far the other way in cutting off all rights or claims as of the date of bankruptcy. Despite the temptation to use a picturesque metaphor, the courts prior to 1938 had been prone to conclude that for some purposes, at least, one who was petitioned *against* was neither civilly nor economically dead. Section 70d recognizes this practical viewpoint and has the added virtue of defining . . . the exact limits under which certain specified transactions will be protected. *Beyond those limits the courts are no longer free to go.*

"*The theory of protected transactions as enunciated by Section 70d creates, of course, an exception to the general rule, now firmly fixed by the Act, that the time of filing the petition is the date of cleavage in bankruptcy.* [fol. 91] Thus the operation of the mere filing of the petition as a *caveat* must give way to this statutory qualification. The draftsmen of the 1938 Act were consistent, however, in their regard for protected transactions. The contemporaneous adoption of Section 63b has made possible the filing of claims by those who contract on a bona fide basis with an involuntary bankrupt before adjudication or the appointment of a receiver.

"*But it must be kept in mind that Section 70d . . . defines the full extent to which bona fide transactions with the bankrupt, after bankruptcy, will be protected.* Subject to the exceptions thus created, *the bankruptcy petition is still a caveat* and persons dealing with the bankrupt thereafter do so at their peril. (emphasis supplied)

A further excellent historical review of "protected transactions" under the Bankruptcy Act is set forth in portions of *Lake* v. *New York Life Insurance Company* (U. S. Court of Appeals 4th Cir. 1954) 218 Fed. Reporter (2nd) 394. We quote below various portions of that decision:

"It has long been the law that the title of a bankrupt to his property passes to the trustee at some point in the course of the proceeding in bankruptcy; and controversies have arisen as to the rights of persons dealing with the bankrupt without notice of the proceeding after it has been instituted. Under the Bankruptcy Act of 1867, R.S. 980 Sec. 5044, title passed to the trustee as of the date of filing the petition; and in *International Bank* v. *Sherman,* 11 Otto. 403, 101 U.S. 403, 25 L.Ed. 866, where a bank without notice loaned money on securities transferred to it by a bankrupt after the bankruptcy proceedings were instituted, the court held that the filing of the petition was a caveat to all the world and that the assignee in bankruptcy was entitled to receive the property.

"Later the Bankruptcy Act of 1898, 30 Stat. 565, U.S. Comp. Stat. 1901, p. 3451, provided that the title to the bankrupt's property vested in the trustee as of the date of adjudication, and it was held in *Mueller* v. *Nugent,* 184 U.S. 1, 22, S.Ct. 269, 46 L.Ed. 405, that under this Act, as under the Act of 1867, the filing of the petition is a caveat to all the world and in effect an attachment and an injunction. Cases of hardship, [fol. 92] however, occurred in which a trustee in bankruptcy sought recovery of money or property belonging to the bankruptcy estate which other persons, without notice of the bankruptcy proceedings, had paid out or transferred on the authority of the bankrupt, and the courts did not give full effect to the pronouncements of the Supreme Court.

. . .

"The uncertainty and confusion of the courts as to when protection should be given to transactions between the bankrupt and innocent third persons after the filing of the petition in bankruptcy led to the amendment of Sec. 70 in the revision of the Bankruptcy statute by the Chandler Act of 1938, and particularly to the addition of subsection d thereof.

. . .

"The new matter in the statute is found in Sec. 70, sub. d, which has a direct bearing on the problem before the court. It provides specifically for certain protected transactions which occur after bankruptcy and either before adjudication or before a receiver takes possession of the bankrupt's property, whichever first occurs.

. . .

"It is obvious that the intent of this enactment is to invalidate transactions not granted specific protection under the Act and thus put to an end the confusion theretofore existing in the decisions. There is almost always some injustice or hardship which attends transactions occurring after the filing of a petition in bankruptcy between the bankrupt, acting wrongfully, and an innocent third person, because the loss must fall either upon the third person or upon the creditors of the bankrupt. Whether the line which has been drawn is the best possible solution of the problem is not for the courts to say. The line has in fact been drawn by competent authority and it is no longer necessary for the courts to make the attempt, which has not been conspicuously successful in the past, to decide cases on the facts as they arise and to draw a fine distinction between transactions which should be protected and those which should not. It is significant that Congress has substituted for the doctrine that the mere filing of a bankruptcy proceeding is a caveat to all the world,

[fol. 93] the specific provision that the taking possession by a receiver or trustee of all or the greater portion of the property of the bankrupt shall constitute public notice and nullify the protective provisions relating to transfers of the bankrupt's property and the payment of indebtedness or delivery of property to him, set out in paragraphs (1) and (2) of Sec. 70, sub. d." 218 F.2nd at pp. 397-399.

Basically, the appellant's argument herein is that unless and until the bank receives *actual* notice of the existence of a bankruptcy the bank should be protected when it cashes the checks of a bankrupt subsequent to the filing of a petition, *whether the same be a voluntary petition or an involuntary petition.* However, even in the case of an involuntary petition in bankruptcy (where there is an hiatus period between the filing of the petition and the adjudication), no further notoriety is given to the fact of adjudication or the appointment of a receiver than occurs when a voluntary petition is filed. Nevertheless, in the case of the involuntary petition, Congress selected two alternative dates for the creditors of protection (whichever was the earlier) (1) the date of adjudication, or (2) in those cases where a receiver takes possession of the property prior to the adjudication, the date the receiver takes such possession. Congress assumed, therefore, that either of these dates were sufficiently notorious events to charge a bank with notice.

III

The second argument in Bank of Marin's appellate brief relies heavily on Section 952 of the California Financial Code, which provides in part as follows:

"Notice to any bank of an adverse claim (the person making such adverse claim being hereinafter in this section called 'adverse claimant') to a deposit stand-

> ing on its books to the credit or to personal property held for the account of any person may be disregarded [fol. 94] until and unless the adverse claimant shall (a) procure and serve upon the bank at the office at which the deposit is carried or the property held a restraining order, injunction, or other appropriate order against the bank . . . or (b) execute and deliver to the bank at the office at which the deposit is carried or the property held a bond in form and with surety acceptable to it and in an amount fixed by the bank . . . Unless such restraining order, injunction, or other appropriate order is obtained, or such bond is given, the bank, notwithstanding such *notice*, may honor the checks . . . without any liability on the part of the bank."

It is the contention of the Bank of Marin that the Trustee in Bankruptcy is included within the meaning of "adverse claimant" as used in Section 952, and that since he failed to comply with the requirements of that statute, the Bank acted properly in honoring the bankrupt's checks. This argument is invalid for several reasons.

First, inclusion of the Trustee in Bankruptcy within the meaning of "adverse claimant" in Section 952 will cause the California statute to be inconsistent with the Bankruptcy Act. Section 70(d) clearly infers that any party with actual notice of the bankruptcy is NOT protected in any event. Section 952, on the other hand, states that even *actual* notice is not enough; that either indemnification or injunction is required. The only way to prevent such an inconsistency is to avoid including the trustee within the meaning of "adverse claimant" in Section 952.

Second, the case of *First National Bank of Arizona* v. *Butler*, 82 Arizona 361, 313 P.2d 421, 62 A.L.R. 2nd 1113 (1957), cited by appellant in his brief, could not be more explicit on this point. In referring to the analogous statute to Cal. Fin. Code Section 952, the court said:

"We hold that the trustee was not an 'adverse claimant' within the meaning of Section 51—535 supra.; hence we find that this statute is nowise controlling."

[fol. 95] Also, appellant's citation of *In Re Fuller,* 294 Fed. 71, as holding that the trustee in bankruptcy is an "adverse claimant" is quite misleading. The court in the *Fuller* case used the term "adverse claimant" in a totally different context; it was not construing the type of statute such as we have in Fin. Code Section 952. Certainly, neither the court in *Fuller* nor any other court would contemplate requiring the trustee to post bond or seek an injunction in order to halt the flow of a bankrupt depositor's funds.

Third, a brief survey of California authorities and law review commentaries reveals no intention whatsoever to include the Trustee in Bankruptcy within the meaning of "adverse claimant". In an article commenting on the new provision of the *Uniform Commercial Code,* Section 3-603, which includes substantially the same requirements as Financial Code, Section 952, an adverse claimant is described as one who bases his claim to the instrument on an allegation such as theft, mistake, fraud, or breach of fiduciary duty; or, he may be a former holder or endorser of the instrument who claims the instrument was improperly taken from him. 65 *Yale L.J.* 807 (1956).

An article in *University of Chicago Law Review* lists these situations where the doctrine of adverse claim against the deposit arises: where funds are wrongfully deposited, where the money has been misappropriated or attained in illegal or voidable transaction, where the deposit itself is a misappropriation, or where the money is deposited by a fiduciary and the adverse claimant asserts himself as beneficial owner. 21 *University of Chicago Law Review,* 135, 136.

Lastly, in an article including the most general and complete discussion of all adverse claim situations, it is pointed

out that the most common situation in the category of protective adverse claims is a claim of a creditor and his [fol. 96] attempts to have the deposit applied to payment of the depositor's debt to him. But the comment expressly makes no mention whatsoever of the Trustee in Bankruptcy as an adverse claimant, although he would seem to be the most apt candidate for this category of adverse claimants. "Conflicting Rights, Duties and Liabilities of Interested Parties upon Assertion of Adverse Claim to Bank Deposits", 51 *Yale L.J.* 986, 987-991 (1942).

Thus, it is quite clear that the notion of adverse claimant as used in Financial Code, Section 952, does not include the Trustee in Bankruptcy.

IV

Appellant next attempts to apply the doctrine of equitable estoppel. In order for this doctrine to be applicable at all, it is necessary to predicate the giving of actual notice by the officers of the bankruptcy court. Since this is the very issue, in this case, it may not be so predicated.

V

The Bank of Marin has argued that the adjudication in the lower court has deprived it of property without due process of law, because it was held liable for honoring checks of its bankrupt depositor subsequent to his adjudication in bankruptcy, despite the fact that it had no actual notice of such an adjudication. There are two answers to this argument.

(A) The Bank's argument that it has been deprived of property without due process of law is *premature,* and is improperly raised in this appeal. The judgment in the lower court has been completely satisfied by Eureka Fisheries, and if this appeal is dismissed, the Bank will not have been deprived of any property whatsoever.

It is true, of course, that there is a possibility that Eureka Fisheries may sue the Bank to recover alleging its

purported right of contribution. However, many adequate [fol. 97] defenses may be interposed by the Bank in such a suit. For example, the Bank may contend that the payee on the checks has been unjustly enriched, and therefore is not entitled to contribution. Or, the Bank may contend that this was money paid out by it by mistake, and that consequently it should not be held liable twice on the same checks. Hence, the court should hesitate in deciding a constitutional issue of such great importance, until it becomes certain that there actually has been a deprivation of the Bank's property.

(B) Should the court find that this issue has not been raised prematurely, the court must then decide the question of whether or not the Bank could possibly be deprived of the property without due process of law.

The landmark case dealing with due process under the Bankruptcy Act is *Hanover National Bank* v. *Moyses,* 186 U.S. 181, 46 L.Ed. 1113 (1902). In response to a contention that the provisions of the Bankruptcy Act constitute a denial of due process in that they fail to provide for adequate notice, the Supreme Court said:

> "Congress may prescribe any regulations concerning discharge in bankruptcy that are not so grossly unreasonable as to be incompatible with fundamental law, and we cannot find anything in this Act on that subject which would justify us in overthrowing its action." 186 U.S. at 192.

Congress had to provide some point after which all transactions with the bankrupt or with his property would be void. In the original Bankruptcy Act of 1867, the filing of the petition was considered as a "caveat to all the world", and thereafter all the bankrupt's property was deemed to be in the custody of the Bankruptcy Court. *Mueller* v. *Nugent,* 184 U.S. 1, 14, 46 L.Ed. 405, 411. However, many injustices occurred as far as persons dealing with the bank-

[fol. 98] rupt prior to his adjudication, and consequently it became clear that a change was needed. In 1898 Congress made such a change and provided that certain good faith transactions between the time of filing of the petition and the moment of adjudication would receive protection. Adjudication was made the final cutoff point, and after that time *all* transactions, regardless of any good faith, were declared invalid. The reason behind this change, and the necessity for it, are ably set out in *Matter of Mertens,* 15 A.B.R. 362, 368, 144 Fed. 818. The court said:

> "The change in the present act, by which the trustee's title is that only which exists at the date of adjudication, removes any uncertainty which arose under the Act of 1867. It was intended, we think, to permit all legitimate business transactions between a debtor and those dealing with him, to be carried out and consummated as freely until he has been adjudicated a bankrupt as though no proceeding were pending. In many cases the proceeding against an alleged bankrupt is unfounded, and for this and other reasons never culminates in an adjudication. While the filing of a petition in bankruptcy is a caveat to all the world, the notice ought not to have the effect of paralyzing all business dealings with the debtor . . ."

In all cases subsequent to *Mertens,* including those cited by appellant in his brief, the courts have been very careful to distinguish between transactions made prior to adjudication, and those made subsequent thereto. While permitting the former, courts have been very quick to strike down the latter. See *In Re Zotti,* 186 Fed. 84, 86 (1911). See also *Matter of Shone & Jaffe,* 10 A.B.R. (ns) 648, 652 (1927), where the court emphasized that protection of those dealing with a debtor lasts only "until he has been adjudicated a bankrupt", and that thereafter all protection would cease.

The courts have been aware that these provisions may cause injustices in certain isolated instances. For example, in *Southern Railway Company* v. *Cole,* 49 G.A. App. 635, [fol. 99] 28 A.B.R. (ns) 587 (1934), a debtor of the bankrupt paid off his debt to him after his adjudication in bankruptcy. Despite the fact that he had had no notice whatsoever of the adjudication, the court compelled him to pay again to the trustee. "An adjudication of bankruptcy is a notorious judicial act of which all persons are bound to take notice." 28 A.B.R. (ns), at Page 588. The court took care to distinguish the cases of *In Re Zotti* (C.C.A. 2nd Cir.) 186 Fed. 84, 26 A.B.R. 234, and *Citizens Union Nat. Bank* v. *Johnson* (C.C.A., 6th Cir.), 286 F. 527, 31 A.L.R. 255, 2 A.B.R. (ns) 927, both relied upon by the appellant, on the ground that the payments made in those cases were made *prior* to the adjudication. Certainly, the Bank of Marin was in no worse position than the legally unsophisticated debtor in *Southern Railway Co.* In fact, the Bank must have been aware that it was not impossible that one of its depositors might go bankrupt. To guard against this possibility, it would not have been a great burden for the Bank to scan the local legal publications which publish daily local adjudications in bankruptcy. Had this been done in the instant case, the honoring of Marin Seafood's checks subsequent to its adjudication in bankruptcy could have been prevented.

Thus, it can be seen that the choice of the moment of adjudication as the cutoff point was not predicated by a concern for providing notice to interested parties. Rather, it was the feeling that during the period of the filing of an involuntary petition and adjudication, there is the danger that an unfounded petition could destroy the business of an alleged bankrupt. This danger is eliminated upon adjudication, and thus after adjudication, no exceptions are made to the trustee's dominion over the bankrupt's property, and good faith on the part of the Bank ceases to be a defense. 70 Harv. L. Rev. 548 (1957). Since the

practical difficulty of obtaining notice of the bankruptcy [fol. 100] would exist no matter where the cutoff point was chosen, Congress simply had to draw the line at the time when the danger of destroying the bankrupt's business no longer existed—i.e. upon adjudication, and the risk of dealing with a check after adjudication in bankruptcy must be regarded as "one of the risks run by anyone who takes a negotiable instrument". 64 Harv. L. Rev. 958 (1951).

With such a rational basis tested by years of experience, it is clear that these regulations go far beyond the minimum requirements of *Hanover National Bank* v. *Moyses,* supra, which provided that any regulations concerning discharge be "not so grossly unreasonable as to be incompatible with fundamental law".

Thus, Congress has chosen a rational basis for attempting to protect the interests of all concerned while still permitting the bankrupt to obtain his discharge. As Remington points out:

> "Much of the usual routine of due process may be clipped short where due and speedy administration of the affairs of an insolvent is the objective, and the liquidation and settlement of his affairs is of paramount, practical importance. 1 *Remington on Bankruptcy* 23.

It is therefore beyond doubt that the time tested provisions of Section 70 of the Bankruptcy Act do not violate the Fifth Amendment. Consequently, the Bank of Marin has not been deprived of property without due process of law.

It is, therefore, submitted that the judgment of the Referee in Bankruptcy was, and is, proper, and should be, by this court, therefore, affirmed.

Respectfully submitted,

Dinkelspiel & Dinkelspiel, By: Harold A. Block,
Attorneys for Trustee.

Dated: August 7, 1964.

[fol. 101-102]

EXHIBIT "A" TO TRUSTEE'S MEMORANDUM OF POINTS AND AUTHORITIES

IN THE UNITED STATES DISTRICT COURT

FOR THE NORTHERN DISTRICT OF CALIFORNIA

SOUTHERN DIVISION

No. 74820

In Bankruptcy

In the Matter of

MARIN SEAFOODS, INC.,

Bankrupt.

NOTICE OF PAYMENT AND CLAIM TO CONTRIBUTION

TO: LYNN J. GILLARD, REFEREE IN BANKRUPTCY: to
JOHN M. ENGLAND, TRUSTEE, AND HIS ATTORNEYS, DINKELSPIEL & DINKELSPIEL: And to
BANK OF MARIN AND ITS ATTORNEYS, FREITAS, ALLEN, McCARTHY & BETTINI:

Take notice that Eureka Fisheries Inc., a corporation, doing business as Eureka Seafoods, has paid the judgment for $2312.82 in the above-entitled matter entered March 31, 1964, and does claim contribution from its joint judgment debtor, Bank of Marin.

Dated: May 19, 1964.

MATHEWS & TRAVERSE

By .....
Attorneys for Eureka Fisheries Inc., a corporation

[fol. 103]

IN THE UNITED STATES DISTRICT COURT

FOR THE NORTHERN DISTRICT OF CALIFORNIA

SOUTHERN DIVISION

No. 74820

In Bankruptcy

[Title omitted]

CLOSING MEMORANDUM OF POINTS AND AUTHORITIES OF BANK OF MARIN—Filed September 23, 1964

Introduction

The Bank of Marin agrees that the issues presented in the Petition for Review are not moot in the legal sense. Nor are they moot as to the Bank of Marin in a practical sense in view of the existing judgment holding the Bank jointly liable with Eureka Fisheries who have demanded contribution from the Bank.

The Bank does, however, object to an order being made deleting that portion of the joint judgment which imposes liability upon the Bank to the Trustee without having this Court determine the issues presented by the Petition for Review. First, it is unlikely that the Court can make such an Order at this time without making a final determination of the issues presented in view of the fact that Eureka Fisheries has paid the sum of $2,312.82 to the Trustee in Bankruptcy and has made a demand for contribution upon the Bank. Such an Order would indeed seriously prejudice the rights of Eureka Fisheries who were entitled to rely upon the Referee's Order holding the Bank jointly liable [fol. 104] with them in paying said sum of $2,312.82 and not petitioning for a review of the judgment as to themselves.

[File endorsement omitted]

To alter such judgment without finding whether the decision of the Referee was legally correct as to the Bank, would in effect impose sole liability upon Eureka Fisheries without permitting them to ask for a review of the Referee's decision.

Secondly, the issues that are presented in the Petition for Review are of such importance to the Bank of Marin and to the banking industry in general, that a final determination of the correctness of the Referee's decision and the basis therefor, insofar as it relates to the Bank of Marin, is of great importance and practical significance.

I.

The Trustee in his Memorandum of Points and Authorities relies heavily upon the fact that Section 18 (f) of the Bankruptcy Act was enacted after the case of *Rosenthal* v. *Guaranty Bank and Trust Co.* (D.C. La. 1956) 139 F. Supp. 730 was decided. The Trustee asserts that as a result, the reasoning and the holding of the *Rosenthal* case are no longer applicable because of the elimination of the time lag between the time of filing a voluntary petition in bankruptcy and the actual adjudication in bankruptcy. However, an examination of the *Rosenthal* case and the Court's Conclusion of Law indicates the bases upon which that decision was predicated are in no way affected by the enactment of Section 18 (f).

"Conclusions of Law:

. . .

"(2) The trustee of the estate of a bankrupt is vested with title of the bankrupt as of date of filing of petition initiating the proceeding. Title 11 U.S.C.A. Section 110.

"(3) The change-over from reorganization proceedings to regular bankruptcy is of no importance here because under the express provisions of the Bankruptcy Act, the

rules applicable to ordinary bankruptcy proceedings insofar as the subject matter of the case is concerned, are made applicable to reorganization proceedings, and the date of adjudication shall be taken to be the date of approval of the petition for reorganization. Title 11 U.S.C.A. Sections 502 and 638.

[fol. 105] "(4) Title 11 U.S.C.A. Section 110 subdivision (d), which is decisive of the issue involved, reads as follows:

'(d) After bankruptcy and either before adjudication or before a receiver takes possession of the property of the bankrupt, whichever first occurs—

. . .

'(5) A person asserting the validity of a transfer under this subdivision shall have the burden of proof. Except as otherwise provided in this subdivision and subdivision (g) of Section 44 of this title, no transfer by or in behalf of the bankrupt after the date of bankruptcy shall be valid against the trustee: *provided, however, that nothing in this title shall impair the negotiability of currency or negotiable instruments.*'

"(5) One of the purposes of the negotiability clause as it appears in subparagraph (5) of subdivision (d), Section 110, Title 11, U.S.C.A., is to protect banks who in good faith, for present equivalent value, in the usual course of their business, and without actual knowledge of the bankruptcy, honors checks drawn on it by the bankrupt and especially is this true when, as here, the checks were drawn before the filing of the petition." (Page 736)

It is apparent that the Court considered the Trustee as having been vested with title of the bankrupt as of the date of the filing of the petition. Furthermore, the Court considered the date of adjudication to be the date of the

approval of the petition for reorganization. This date was prior to the dates upon which the Bank honored checks previously drawn by the bankrupt. Even so, the Court held that the Bank was protected where it honored checks in good faith without actual knowledge of the pending bankruptcy proceedings.

The Trustee goes to great lengths to attempt to establish that the protective provisions of Bankruptcy Action Section 70d (5) do not apply to the situation presented herein. However, the Rosenthal case, supra, is unequivocal in holding that Section 70d (5) was intended to protect a bank which honors a bankrupt depositor's check in good faith without actual knowledge of the bankruptcy proceeding.

> "The trustee particularly directs the court's attention to subparagraph (5) of Title 11 U.S.C.A. Section 110, subdivision d, which he says plainly and expressly states that except as provided in subdivision d and in subdivision g of Section 44 (which latter subdivision relates to real estate and has no bearing here), no other transfer after the date of the bankruptcy shall be valid against the trustee, and of course, he argues, the only [fol. 106] exceptions stated in subdivision are that the payments must be made both before adjudication and without notice of the pending proceeding.
>
> "This argument is not without merit and were it not for the fact that there is appended to that section the proviso 'that nothing in this title shall impair the negotiability of currency or negotiable instruments', we would be inclined to agree. Since no court decision has been called to our attention and none having been found interpreting the meaning or purpose of this provision, the matter must be considered res integra. Where the bankruptcy occurs the bank upon which the bankrupt drew a check prior to the date of the bankruptcy finds himself caught in the intermeshing of two highly complicated systems of law. Traditionally, it is

> the primary function of the Bankrupty Act to protect the creditors, to marshal the assets, and to distribute them among the creditors equitably and ratably in accordance with their respective rights and interests. *Negotiability tries to give the bank the maximum assurance that it will be able to cash the check without any defenses being interposed.* Expansion of bankruptcy in some senses indisputably hinders the flow of commercial paper. *In the absence of any prior interpretation, we agree with counsel for defendants that one of the purposes of the 'negotiability' provision in the Bankruptcy Act was to protect a bank in a case of this kind, if the bank was in good faith and had no 'actual knowledge' of the pending bankruptcy.*" (At page 734) (emphasis added).

Not only is the negotiability of a check impaired as to the Bank but it is further impaired in view of the fact that the payee of a check (Eureka Fisheries) is a holder in due course. *Flores* v. *Wood Specialties, Inc.*, 138 C.A. 2d 763 (1956). To hold that a payee of a check to whom said check was negotiated prior to the filing of a voluntary petition in bankruptcy is liable either to the Trustee in Bankruptcy (assuming that there has been no preference or fraudulent transfer) definitely destroys the negotiability of the check and violates California Civil Code Section 3138 which provides:

> "A holder in due course holds the instrument free from any defect of title of prior parties, and free from defenses available to prior parties among themselves, and may enforce payment of the instrument for the full amount thereof against all parties liable thereon."

II.

The Trustee contends that the inclusion of the Trustee within the purview of California Financial Code Section 952

would cause that Section to be inconsistent with the Bankruptcy Act in that Section 70 (d) of the Bankruptcy Act [fol. 107] provides that "actual knowledge" is all that is required under that Act to prevent a transfer from being valid, whereas Section 952 requires a Court Order or an indemnity bond to be served upon the bank. However, the Trustee fails to consider the application of Section 952 in conjunction with the last phrase of Section 70 d (5) which provides:

> "That nothing in this act shall impair the negotiability of currency or negotiable instruments."

It is clear that where a negotiable instrument such as a check is involved there is no provision in the Bankruptcy Act providing for notice to the bank upon whom the check was drawn. Lacking such a provision State law applies thus requiring the Trustee in Bankruptcy to comply with Section 952 if he is to hold the bank liable for honoring a check drawn by the bankrupt upon sufficient funds.

Furthermore, "actual knowledge" only comes in to play if the transaction falls within the ambit of Sections 70 d (1) and 70 d (2). Even within those provisions there would be no inconsistency between Financial Code Section 952 and the Bankruptcy Act if Section 952 was applied to persons *not* having "actual knowledge" of the pending bankruptcy proceeding.

The Trustee in Bankruptcy of a bankrupt depositor is most certainly an "adverse claimant" to a deposit held by a bank upon which a check has been drawn and negotiated to a payee prior to bankruptcy and which check has been presented to the bank for payment after bankruptcy. The bank is under a legal obligation to honor the check or become liable to the depositor in damages. *Weaver* v. *Bank of America,* 59 Cal. 2d 432 (1963).

Section 952 is a similar statute to that recommended by the American Bankers Association which statute has been adopted in numerous states and imposes no limitation upon

the persons who qualify as "adverse claimants". Paton's Digest of Legal Opinions (1942) Vol. II, page 1656-1658; "Brady on Bank Checks" (3rd ed. 1962) page 293; *Gendler* v. *Sibley State Bank,* 62 Fed. Supp. 805 (1945). The asser- [fol. 108] tion that a Trustee in Bankruptcy is to be excluded is without any basis whatsoever. The case of *First National Bank of Arizona* v. *Butler,* 82 Ariz. 361, 313 P. 2d 421 (1957) is readily distinguishable as pointed out in the Opening Memorandum of Bank of Marin at page 6.

A general discussion is contained in *Gendler* v. *Sibley State Bank,* supra, at page 811:

> "Because of the difficult situation in which a bank is placed when an adverse claim is made by a third party to a deposit standing in the name of another, the American Bankers Association a number of years ago recommended a statute to protect banks in such cases. The statute so recommended provides in substance that when a third party gives notice to a bank of an adverse claim to a deposit, that the bank does not have to recognize such claim until it is directed to do so by proper Court order or unless a proper indemnifying bond is furnished to the bank."

III.

A judgment has been rendered against the Bank of Marin and Eureka Fisheries jointly for the sum of $2,312.82. Eureka Fisheries has paid said sum and has filed a Claim to Contribution in the bankruptcy action demanding contribution from the Bank of Marin. It is apparent that the Bank is not premature in raising the constitutional argument that its property has been taken without due process of law. As the Trustee points out in pages 3 and 4 of his Memorandum of Points and Authorities, the Bank would be precluded by the doctrine of res judicata from raising the issue in defense of a subsequent suit instituted by Eureka Fisheries. (See: *Estate of Merrill,* 29 Cal. 2d 520 (1946);

Metcalf v. *Drew*, 75 C.A. 2d 711 (1946)). As opposed to being premature, the constitutional question raised by the Bank is timely and in fact might be waived if the Bank does not raise it at this time.

The Trustee evades the constitutional issue presented. The mere fact that Congress may have decided that adjudication was to be the final cutoff point after which all transactions are to be declared invalid, does not thereby relieve the Bank or any other person in a similar position of the protection of the due process clause of the Fifth Amendment. As set forth in the Bank's Opening Memorandum of Points and Authorities, the due process clause is applicable [fol. 109] to the Bankruptcy Act and bankruptcy proceedings. (Page 9.)

Furthermore, the Trustee has cited no case that is analagous to the situation presented. Here the Bank is under a legal obligation to honor a check that is properly drawn upon sufficient funds. *Weaver* v. *Bank of America*, 59 Cal. 2d 432 (1963). However, if the Bank honors such a check without actual knowledge of the bankruptcy proceedings, the Trustee would have this Court hold that the Bank is liable to the Trustee. No cases cited by the Trustee present the situation where a party is confronted with liability if it selects either of two alternatives afforded and is under a legal obligation to comply with both such alternatives. As pointed out in the Bank's Opening Memorandum of Points and Authorities (page 7), it is not sufficient to say that the Bank would not incur liability to the depositor if the depositor had in fact filed a voluntary petition in bankruptcy if the Bank failed to honor the bankrupt's check. To take this course of action, the Bank would necessarily have to have notice of the filing of the petition in bankruptcy, which notice it does not have at the time it must decide which course to follow.

It is conceded by the Trustee that no notice of adjudication other than the mere filing of the voluntary petition in bankruptcy is given to the Bank and that the Bankruptcy

Act requires no further notice. To contend that this is notice reasonably calculated, under all the circumstances, to apprise the Bank of the pendency of the bankruptcy proceedings, is preposterous and wholly unrealistic. Under this view, to receive timely notice of the filing of a voluntary petition in bankruptcy by one of its depositors, the Bank would have to post a person in every office of the Clerk of the District Court to momentarily apprise the Bank of the filing of voluntary petitions by depositors. The obvious unreasonableness of this course of action is apparent.

The Trustee further contends that a bank is afforded sufficient notice by means of local legal publications. This is equally unrealistic. First, the Bankruptcy Act does not require that all adjudications in bankruptcy be published each day and there is no assurance that private publishing companies will continue without interruption to accomplish such publication.

[fol. 110] Secondly, it is highly doubtful that the constitutional deficiencies in the Bankruptcy Act relating to the giving of notice of adjudications can be cured by the independent acts of a private publishing company under no compulsion to make such publications.

Thirdly, such an assertion assumes that all banks, no matter where they are located, subscribe to such legal publications. It must be pointed out, that the Bank would have to subscribe to legal publications published in every City in the United States where there exists a Clerk of the District Court in order to keep itself apprised of all bankruptcy filings by any one of its depositors. A bank would then have to examine each publication every day to determine whether or not any of its depositors have been adjudicated bankrupt.

Fourthly, even if the Bank did subscribe to all of such publications and examined such publications, there is at least a one or two day lag in time between the date of adjudication and the date the Bank would receive such publication. During this period of time many thousands

of checks would be honored by the Bank, any of which could have been drawn by a depositor who had filed a voluntary petition in bankruptcy that day or the day before. As to these persons, even if the Bank assumed the unreasonable burden of advising itself of all bankruptcy filings in every district in the United States by reviewing legal publications, the Bank would have no notice of the adjudication.

In conclusion, the Bank of Marin respectfully submits that there is no legal basis for the holding of the Referee in Bankruptcy in this proceeding. Furthermore, if such a holding is sustained by this Court, the entire banking industry will have to revise its procedure for honoring checks which revision will necessarily delay and impair commercial transactions and the passing of negotiable instruments.

Respectfully submitted,

Freitas, Allen, McCarthy & Bettini, Attorneys for Bank of Marin.

[fol. 111] Proof of Service by Mail (omitted in printing).

[fol. 112]

IN THE UNITED STATES DISTRICT COURT

FOR THE NORTHERN DISTRICT OF CALIFORNIA

SOUTHERN DIVISION

No. 74820

In Bankruptcy

[Title omitted]

ORDER AFFIRMING REFEREE'S ORDER—October 26, 1964

Bank of Marin has petitioned for a review of the referee's order in the above entitled action adjudging it jointly liable to the trustee for $2,312.82. Petitioner argues that

because of the adverse effects on the banking industry of the referee's interpretation of the statutory bankruptcy scheme and because of possible constitutional objections a contrary construction should prevail.

After a careful review of the relevant cases and authorities and a detailed evaluation of facts alleged in the briefs filed herein, this Court has concluded that under [fol. 113] the circumstances the referee's order was proper. The findings of fact and reasoning contained in his opinion of February 24, 1964 are hereby adopted and the judgment of March 31, 1964 is hereby affirmed.

Dated: October 26, 1964.

Albert C. Wollenberg, United States District Judge.

[File endorsement omitted]

[fol. 114]

IN THE UNITED STATES DISTRICT COURT

FOR THE NORTHERN DISTRICT OF CALIFORNIA

SOUTHERN DIVISION

No. 74820

In Bankruptcy

[Title omitted]

NOTICE OF APPEAL—Filed November 20, 1964

Notice is hereby given that the Respondent, Bank of Marin, hereby appeals to the United States Court of Appeals for the Ninth Circuit from the Order Affirming Referee's Order dated October 26, 1964 and filed October 27, 1964, the Referee's Order and Judgment thereon being dated March 31, 1964.

The names of the parties to this Order and the names and addresses of their respective attorneys are as follows:

Bank of Marin, Appellant herein, who is represented by Freitas, Allen, McCarthy & Bettini, 960 Fifth Avenue, San Rafael, California;

John M. England, Trustee in Bankruptcy herein, who is represented by Dinkelspiel and Dinkelspiel, 405 Montgomery Street, San Francisco, California;

Eureka Fisheries, Inc., represented by Matthews & Travers, 3509 Professional Building, Eureka, California.

Dated: November 19, 1964.

Freitas, Allen, McCarthy & Bettini, Attorneys for Bank of Marin.

[File endorsement omitted]

[fol. 115]

IN THE UNITED STATES DISTRICT COURT

FOR THE NORTHERN DISTRICT OF CALIFORNIA

SOUTHERN DIVISION

No. 74820

In Bankruptcy

COST BOND ON APPEAL—Filed November 20, 1964

The Bank of Marin, appellant, herewith deposits with the Clerk of the United States District Court for the Northern District of California, Southern Division, the sum of Two Hundred Fifty Dollars ($250.00) in cash as and for the bond for costs on appeal to the Court of Appeals for the Ninth Circuit from the Order entered in this action on October 26, 1964, to secure the payment of costs if the appeal is dismissed or the Judgment affirmed, or the pay-

ment of such costs as the Court of Appeals may award if the Judgment is modified.

Dated: November 19th, 1964.

Bank of Marin, By Burton R. Kirchner, Vice President.

[File endorsement omitted]

[fol. 116]

IN THE UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

No. 19776

In Bankruptcy

BANK OF MARIN,

vs.

JOHN M. ENGLAND, Trustee in Bankruptcy.

In the Matter of

MARIN SEAFOODS, INC. and EUREKA FISHERIES, INC.

STATEMENT OF POINTS ON WHICH APPELLANT INTENDS TO RELY ON APPEAL—Filed January 8, 1965

The points on which Appellant, Bank of Marin, intends to rely on appeal are:

1. The order of United States District Judge affirming Referee's order of March 31, 1964, adjudging the Bank of Marin jointly liable to the Trustee for the sum of $2,312.82, is in error;

[File endorsement omitted]

2. Conclusion of Law No. 4 of the Referee, that the Trustee herein is entitled to a judgment in the sum of $2,312.82 against the Bank of Marin and Eureka Fisheries, Inc. dba Eureka Seafoods, jointly, is clearly erroneous;

3. Conclusion of Law No. 5 of the Referee, that the lack of actual knowledge of the Bank of Marin of the filing of the voluntary petition in bankruptcy by Marin Seafoods, Inc., affords the Bank of Marin no protection against the Trustee's claim herein, is clearly erroneous;

4. The judgment entered by the Referee upon the Find-
[fol. 117] ings of Fact and Conclusions of Law on March 31, 1964, adjudging that the Trustee have judgment against the Bank of Marin and Eureka Fisheries, Inc., dba Eureka Seafoods, jointly, for the sum of $2,312.82 is in error;

5. The conclusion of the United States District Judge and the Referee in Bankruptcy that title to the property of a bankrupt, including the deposits of the bankrupt with the Bank of Marin, rests in the Trustee as of the date of the bankruptcy petition pursuant to the provisions of Section 70a of the Bankruptcy Act, is in error;

6. The conclusion of the United States District Judge and the Referee in Bankruptcy that no provision in the Bankruptcy Act protects a bank which after adjudication honors checks of the bankrupt drawn prior to bankruptcy, is in error;

7. The conclusion of the United States District Judge and the Referee in Bankruptcy that all transfers not given specific protection under the Bankruptcy Act are absolutely banned, is in error;

8. The conclusion of the United States District Judge and the Referee in Bankruptcy that no provision contained in Bankruptcy Act Section 70d affords protection for a bank which after adjudication honors checks of the bankrupt, is in error;

9. The conclusion of the United States District Judge and the Referee in Bankruptcy that the recipient of such funds after adjudication merely holds property, title to which is vested in the Trustee, is in error;

10. The conclusion of the United States District Judge and the Referee in Bankruptcy that the facts herein do not show the Bank of Marin ever had any claim to funds deposited with it after adjudication of the bankrupt is in error.

Dated: January 6, 1965.

Freitas, Allen, McCarthy & Bettini, Attorneys for Bank of Marin.

[fol. 119]

IN THE UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

Before: Hamley, Jertberg & Merrill, Circuit Judges.

MINUTE ENTRY OF ARGUMENT AND SUBMISSION—
August 6, 1965

This cause coming on for hearing, Edgar B. Washburn, argued for the appellant, and Thomas B. Donovan, argued for the appellee, thereupon the Court ordered the cause submitted for consideration and decision, pending the filing of further briefs in twenty days.

[fol. 120]

IN THE UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

Before: Hamley, Jertberg & Merrill, Circuit Judges.

MINUTE ENTRY OF ORDER DIRECTING FILING OF OPINION AND FILING AND RECORDING OF JUDGMENT—October 28, 1965

Ordered that the typewritten opinion this day rendered by this Court in above cause be forthwith filed by the Clerk and that a judgment to be filed and recorded in the minutes of this Court in accordance with the opinion rendered.

[fol. 121]

IN THE UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

No. 19,776

BANK OF MARIN, Appellant,

vs.

JOHN M. ENGLAND, Trustee in Bankruptcy in the matter of MARIN SEAFOODS, INC. and EUREKA FISHERIES, INC., Appellee.

Appeal from the United States District Court for the Northern District of California, Southern Division.

Before: Hamley, Jertberg and Merrill, Circuit Judges.

HAMLEY, Circuit Judge:

OPINION—October 28, 1965

Bank of Marin appeals from a district court judgment affirming an order of a referee in bankruptcy holding the bank and Eureka Fisheries, Inc., jointly liable to a trustee in bankruptcy for the sum of $2,312.82. The sole question presented is whether a bank which honored checks of a depositor after the depositor had filed a voluntary petition

in bankruptcy is liable to the trustee in bankruptcy for the amount of the checks paid where the bank had no notice of the bankruptcy proceeding.

The relevant facts are not in dispute. Between August 27, 1963, and September 17, 1963, Marin Seafoods drew and delivered five checks in favor of Eureka Fisheries upon its commercial account with Bank of Marin, San Rafael, California. The total amount of the checks was $2,318.82. On September 26, 1963, before these checks had been presented to the bank for payment, Marin Seafoods filed a voluntary petition in bankruptcy. The petition was filed [fol. 122] in the United States District Court for the Northern District of California, Southern Division. John M. England was appointed as receiver and so acted until October 20, 1963, at which time he became trustee for the bankrupt.

On the date of the filing of the petition, sums of money in excess of $3,200 were due and owing Marin Seafoods from customers for merchandise previously delivered. Beginning on the day after the filing of the petition, and continuing for several days, Marin Seafoods, through its principal officer, collected portions of these outstanding accounts receivable and deposited them in the company's commercial account at the bank. On October 2, 1963, the checks which Marin Seafoods had drawn and delivered to Eureka Fisheries prior to the filing of the petition, were duly presented to the bank by Eureka Fisheries for payment, and were paid.

At the time the bank paid these checks it had received no notice, and had not otherwise obtained knowledge of the filing of the petition in bankruptcy. The bank was not informed of the pending bankruptcy proceeding until October 3, 1963, when it received a letter, dated October 2, 1963, from the receiver. This was one day after the bank had honored the checks referred to above.

Proceeding under section 2(a) of the Bankruptcy Act (Act), 52 Stat. 842 (1938), as amended, 11 U.S.C. § 11(a)

(1964), the trustee applied to the referee for a turnover order. The trustee sought to require the bank to pay over to the trustee a sum of money equivalent to the sum paid by the bank to Eureka Fisheries on October 2, 1963. In the alternative he sought relief against Eureka Fisheries. A show cause proceeding ensued, resulting in the entry of an order by the referee, supported by findings of fact and conclusions of law. The referee determined that the bank and Eureka Fisheries were jointly liable to the trustee for the sum of $2,312.82, the amount paid by the bank to Eureka Fisheries.

In so ruling, the referee held that the bank's lack of knowledge of the filing of the voluntary petition in bankruptcy by its depositor Marin Seafoods, afforded the bank no protection. Eureka Fisheries paid the total amount of $2,312.82 to the trustee and then filed with the bankruptcy court, and served upon the bank, a demand for contribution. The bank petitioned for a review of the referee's [fol. 123] order, and on such review, that order was affirmed. This appeal by Bank of Marin followed.

In seeking recovery of the stated amount from the bank, the trustee relied upon section 70(a) of the Act, 52 Stat. 879 (1938), as amended, 11 U.S.C. § 110(a) (1964). This section provides, in pertinent part, that, upon his appointment and qualification, a trustee in bankruptcy shall be vested "by operation of law" with the title of the bankrupt as of the date of the filing of the petition initiating a proceeding in bankruptcy, with exceptions not here material, to described kinds of property wherever located. Among the kinds of property so described, the statute includes:

> "... (5) property, including rights of action, which prior to the filing of the petition he [bankrupt] could by any means have transferred or which might have been levied upon and sold under judicial process against him, or otherwise seized, impounded, or sequestered: *Provided*, ... [not here material]."

This provision of the Act, considered by itself, would appeal to support the trustee's application for a turnover order against the bank. The bank, however, contends that notwithstanding this statute, it should be held that a bank is not liable to a trustee in bankruptcy when, in good faith, and without actual knowledge of the bankruptcy proceedings, it honors the checks of a bankrupt depositor in the regular course of business after the adjudication of bankruptcy. As authority for this view, the bank cites *Rosenthal* v. *Guaranty Bank & Trust Co.*, D.C. La., 139 F.Supp. 730, stating that the holding in that case is "determinative" of this appeal.[1]

In *Rosenthal,* on facts quite similar to those of the case before us, the court held that the proviso of section 70(d)(5) of the Act, 52 Stat. 882 (1938), 11 U.S.C. § 110(d)(5), providing that nothing in the Act " . . . shall impair the nego- [fol. 124] tiability of currency or negotiable instruments . . . " protects a bank in such circumstances.[2]

As indicated by the introductory words of section 70(d), all of that subsection applies only to transactions taking place during the interval, if any, between the filing of a petition in bankruptcy and the adjudication or the taking

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[1] It would perhaps have been better if the bank had referred to the *Rosenthal* case as "persuasive". In the judicial scheme of things, a district court decision which has not withstood the acid test of appellate review cannot be regarded as authoritative, much less dispositive of an appeal, but it may well be persuasive.

[2] Section 70(d)(5) reads:

"(d) After bankruptcy and either before adjudication or before a receiver takes possession of the property of the bankrupt, whichever first occurs—

. . . .

"(5) A person asserting the validity of a transfer under this subdivision shall have the burden of proof. Except as otherwise provided in this subdivision and in subdivision (g) of section 44 of this title, no transfer by or in behalf of the brankrupt after the date of bankruptcy shall be valid against the trustee: *Provided, however,* That nothing in this title shall impair the negotiability of currency or negotiable instruments."

of possession by a receiver, whichever first occurs. But, in the case of voluntary petitions in bankruptcy, such as the one before us, there is no such interval, because the filing of a voluntary petition operates as an adjudication. Section 18(b) of the Act, 73 Stat. 109 (1959), 11 U.S.C. § 41(b) (1964). Therefore section 70(d)(5) of the Act, relied upon by the court in *Rosenthal,* can have no application here.[3]

Moreover, the presentation of a check to the drawee for payment, and the payment thereof, is not a negotiation of the check.[4] If it is not negotiation, an order declaring in- [fol. 125] valid the presentation and payment is not impairment of negotiation. Accordingly, the "negotiability" proviso of section 70(d)(5) has no application.[5]

We conclude that the "negotiability" proviso of section 70(d)(5) does not protect the Bank of Marin under the circumstances of this case.

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[3] Earlier cases in which banks were protected in paying checks all involved payments made after filing of the bankruptcy petition but prior to adjudication. See *Citizens' National Bank* v. *Johnson,* 6 Cir., 286 Fed. 527; *Matter of Retail Stores Delivery Corp.,* D.C.N.Y. 11 F.Supp. 658.

[4] See *Shammas* v. *Boyett,* 114 Cal.App.2d 139, 249 P.2d 880, 883; *Fidelity & Deposit Co. of Maryland* v. *Marion Nat'l Bank,* 116 Ind. App. 453, 64 N.E.2d 583; *Aurora State Bank* v. *Hayes-Eames Elevator Co.,* 88 Neb. 187, 129 N.W. 279; *First Nat'l Bank* v. *United States Nat'l Bank,* 100 Or. 264, 197 P. 547, 555; Seligson, *Creditors' Rights,* 32 N.Y.U.L.Rev. 708, 730-31 (1957); 4 Collier, *Bankruptcy* § 70.68 at 1502-03 n. 3 (14th ed. 1964); Britton, *Bills and Notes,* 118 (2d ed. 1961). Similarly, a drawee bank which has paid the check does not become a holder in due course. *Central Bank and Trust Co.* v. *General Finance Corp.,* 5 Cir., 297 F.2d 126, 128-29.

[5] It should also be noted that *Rosenthal* was decided in 1956, which was prior to the enacting of section 18(f) of the Act, making the filing of a voluntary petition in bankruptcy an automatic adjudication. However, for the purpose of applying chapters I through VII of the Act, the court in *Rosenthal* treated the approval of the petition for reorganization under chapter X as equivalent to adjudication pursuant to section 102 of the Act, 52 Stat. 883 (1938), 11 U.S.C. § 502 (1964). We therefore do not regard the fact that *Rosenthal* was decided prior to the enactment of section 18(f) as a sound basis for distinguishing that case.

The bank also contends that, in California, a trustee in bankruptcy must give a bank notice of the bankruptcy by complying with section 952 of the California Financial Code before he can hold the bank liable for honoring checks of the bankrupt.

Section 925 provides that notice of an adverse claim to bank deposits may be disregarded until the adverse claimant obtains a restraining order, injunction or other court order against the bank; without such an order the bank may honor checks drawn by the depositor or allow withdrawals by him without incurring liability to the adverse claimant. The bank contends that since the Bankruptcy Act makes no provision for notice to banks, state law should apply to fill this gap. The trustee gave no notice in this case, nor did he make any attempt to comply with section 952.

A claim of this kind, made by the trustee in bankruptcy for a bankrupt depositor, is not an "adverse claim," within the meaning of such a statute. *First National Bank of Arizona* v. *Butler,* 82 Ariz. 361, 313 P.2d 421. Thus, even overlooking inconsistencies between section 952 and the Bankruptcy Act,[6] the California statute does not undermine the district court order under review.

[fol. 126] The bank further argues that a court of bankruptcy is governed by equitable principles and, applying those principles to this case, must protect the bank from incurring liability for honoring checks of a depositor where it had no notice of the bankruptcy of the depositor.

Under the trustee's theory of the case the bank must, in order to avoid liability, keep itself informed of the pos-

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[6] Section 70(d) of the Act removes protection from transactions where actual notice is present, while under section 952 the bank is protected even though there is actual notice if the remaining statutory steps have not been taken. The bank argues, however, that this inconsistent provision of section 952 is severable leaving "at least" a requirement of actual notice as a requisite to liability under section 952.

sibility of bankruptcy proceedings involving a depositor. According to the bank, this will require it to keep advised momentarily of bankruptcy filings. This burden is enhanced by the fact that filing in any district court in the United States will have the same effect. The steps demanded for protection are cited as impractical and otherwise burdensome.

The bank's dilemma is real since it is under a duty to depositors to honor checks which are validly drawn; at the same time there is always the possibility that the depositor, without the knowledge of the bank, has become the subject of bankruptcy proceedings. The hardship to the bank of keeping itself apprised of developments in the bankruptcy court is contrasted with the relatively light burden that a notice requirement would place upon the trustee. The trustee or receiver, upon filing, is informed of the bankrupt's accounts and deposits; and notification by him to the bank would be relatively simple.

The trustee, however, takes the position that there would be no great hardship resulting to banks from a ruling imposing liability in this case. It is argued that banks have a vital interest in the credit position of depositors and that banks are well equipped to evaluate, interpret and discover factors affecting the financial well-being of depositors. The trustee cites the reviewing of local legal publications as a method of keeping abreast of bankruptcies. Also the trustee feels that keeping posted outside the immediate area would not be an insurmountable burden. In addition, it is argued that the bank has assumed this risk of doing business and can easily pass the cost of surveillance on to its customers.

Upon considering the respective arguments, we think the bank makes out a strong case for hardship and impracticability insofar as the timely discovery of bankruptcy proceedings involving depositors is concerned. We are not as certain that the problem is one which threatens great and unprotectible financial liability. The fact that

[fol. 127] our case, and *Rosenthal,* appear to be the only reported cases dealing with this particular problem is some indication that it is not one which will frequently confront banks. Moreover, it would seem that the risk, such as it is, may ordinarily be taken into account as a cost of the business and financed as such.

It is true that courts of bankruptcy exercise certain equity powers.[7] But there is no room for equitable relief of a kind which is expressly foreclosed by the Act. Section 70(d)(5), quoted in note 2, above, specifically provides that "Except as otherwise provided in this subdivision and in subdivision (g) of section 44 of this title [section 21(g) of the Act] . . ." no transfer by or in behalf of the bankrupt after the date of bankruptcy shall be valid against the trustee.[8] Neither subdivision (d) of section 70, nor subdivision (g) of section 21, authorize transfers of the kind involved in this case. Equitable relief which would, as against the trustee, validate the bank's transfer to Eureka Fisheries, would thus run counter to section 70(d)(g), and is necessarily precluded.

The California Bankers Association, appearing in this court as *amicus curiae,* joins the bank in all of the contentions discussed above. It also presents the additional argument that the failure of the trustee to revoke the bankrupt's order for the payment of funds on deposit with the Bank of Marin bars the trustee from recovery against the bank.

The gist of this argument is as follows: (1) under section 70(a)(5) of the Act, a trustee in bankruptcy succeeds only to such rights as the bankrupt possessed at the time of the bankruptcy petition, and is subject to all defenses

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[7] Section 2(a) of the Act, 52 Stat. 842 (1938), as amended, 11 U.S.C. § 11(a); *Pepper* v. *Litton,* 308 U.S. 295; *Local Loan Co.* v. *Hunt,* 292 U.S. 234.

[8] The "negotiability" proviso to this subsection has already been discussed.

and equities which might have been asserted against the bankrupt but for the filing of that petition; (2) in California an ordinary depositor does not have title to any specific funds deposited in a bank, the relationship of bank and depositor, founded upon contract, being that of debtor and [fol. 128] creditor; (3) under that contract, a bank has both the right and duty to honor checks of its depositors properly drawn and duly presented, unless the depositor provides the bank with notice of the revocation of his order for payment prior to the time his checks are accepted by the bank; (4) absent the giving of a timely "stop payment" order such payment operates to discharge the bank's obligation, and the depositor has no right to recover the amounts paid; and (5) under the premise set forth at the outset, the trustee is subject to the same defense.

The bankruptcy of a drawer operates as a revocation of the drawee's authority.[9] Such revocation is not dependent upon or subject to notice to the drawee, since the trustee is immediately vested with the title of the bankrupt by operation of law. The parties to a depositor's contract with a bank are chargeable with knowing this when they enter into the contract. These circumstances constitute an implied exception to the contractual obligation of the bank to honor checks unless and until a "stop payment" notice is received. The asserted bank defense based upon lack of a "stop payment" notice is therefore not available against a trustee in bankruptcy in the case of the bankruptcy of the drawer.

Finally, both the bank and *amicus curiae* contend that the district court order under review deprives the bank of due process of law as guaranteed by the Fifth Amendment. Two aspects of this Constitutional argument are presented, the first being that the due process clause forbids imposing

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[9] *Harrison State Bank* v. *First National Bank*, 116 Neb. 456, 218 N.W. 92; *Guthrie Nat'l Bank* v. *Gill*, 6 Okla. 560, 54 Pac. 434; Brady, *Bank Checks*, 25 (3rd ed. 1962).

liability upon a bank unless it has received reasonable notice of the bankruptcy proceeding.

In support of this view, *Mullane* v. *Central Hanover Bank & Trust Co.*, 339 U.S. 306, and several other decisions are cited. In *Mullane*, the question involved was whether adequate notice was given to a person of litigation wherein his rights were being litigated. Prior to the turnover proceedings, however, the rights of the Bank of Marin were not being adjudicated in the bankruptcy proceedings before us. Up to then, the rights of the bank were not affected by any order entered by the referee; the property of the bankrupt was vested in the trustee by operation of law. The [fol. 129] rule as to notice set forth in *Mullane* and similar cases, is therefore inapplicable here.

In *Lambert* v. *California*, 355 U.S. 225, also cited by the bank, the Court held a statute unconstitutional which imposed criminal liability not for an affirmative act, but for the failure of a convicted felon to register despite lack of notice of the requirement. Since the basis for the bank's liability to the trustee cannot be equated with the violation of a criminal statute, *Lambert* is not in point.

The bank also places reliance upon *Hanover Nat'l Bank* v. *Moyses*, 186 U.S. 181. There, a creditor asserted that he had not been adequately notified of the filing and adjudication of a voluntary bankruptcy. But, as in *Mullane* and most of the other decisions cited by the bank, the rights of the creditor in *Moyses* were being adjudicated in the bankruptcy proceeding.

We do not believe that *Moyses* should be extended past its holding that the creditors of a bankrupt are entitled to reasonable notice of the bankruptcy proceedings.[10] The filing of a bankruptcy petition has long been regarded as a *caveat* to all the world. *Mueller* v. *Nugent*, 184 U.S. 1, 14. Likewise, adjudication has been held to be notice to the world, thus invalidating transactions involving the debtor's

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[10] In *Moyses* it was held that the creditor had received sufficient notice.

property occurring after adjudication. *J.S. & J.F. Sterling, Inc.* v. *Birkhahn,* 3 Cir., 30 F.2d 492, 495; 4 Collier, *Bankruptcy,* § 70.66 at 1498 (14th ed. 1964).

Congress may not proceed in complete disregard of the property rights of those dealing in good faith with bankrupts. It may, however, enact legislation balancing bankruptcy objectives with the interests of those dealing in good faith with a bankrupt. Section 70(d) of the Act, we believe, demonstrates that Congress has, in this balancing process, taken into account the latter interests and has accommodated them to the extent deemed feasible having in view the desirability of speedy, economical and effective bankruptcy adminstration.[11]

[fol. 130] In our opinion, the order under discussion does not offend the due process clause, insofar as notice to the bank is concerned.

This brings us to the second facet of the Constitutional argument presented by the bank and *amicus curiae.* This is the contention that the due process clause prohibits imposing liability upon the bank because to do so would require the bank to pay a single debt twice. There is a strong Constitutional policy against requiring the double payment of the same debt. See *Western Union Telegraph Co.* v. *Pennsylvania,* 368 U.S. 71.

The argument for the bank is premised upon these propositions: the relationship of a bank to its depositor is that of debtor and creditor; the bank is obligated to discharge its indebtedness by honoring checks drawn by depositors; and failure to honor such checks results in liability to the depositor. These propositions are not challenged by the trustee for they are well established. Next the bank argues that in honoring the checks drawn by the bankrupt, it discharged its indebtedness in accordance with its obligation

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[11] See *Lake* v. *New York Life Insurance Co.,* 4 Cir., 218 F.2d 394, 397-99; 4 Collier, *Bankruptcy,* §§ 70.66, 70.67, pages 1494-1501 (14th ed. 1964), commenting on the legislative history of section 70(d).

to its depositor. From this, the conclusion is drawn that to require a second payment now to the trustee is a violation of the Fifth Amendment.

As we have already seen, at the time the checks were honored, title to the deposits was vested in the trustee by virtue of section 70(a). From the moment of filing the petition, the bank's duty with regard to the deposits was owed to the trustee, not to the bankrupt and not to the payee of the checks. We have already held that, in legal contemplation, the filing was sufficient notice to those subsequently dealing with the bankrupt's assets. Accordingly, and regardless of actual notice, the bank's obligation to honor the checks disappeared before it paid them. Therefore, in paying the checks when presented by Eureka Fisheries, the bank was not paying a debt for which it was obligated. It follows that if as a result of this judgment the bank pays any part of the checks, it will not be paying the same debt twice.[12]

[fol. 131] The bank characterizes its position as analogous to a garnishee who has paid his creditor without notice of garnishment. A garnishee is not liable to the garnishor in such circumstances. *Harris* v. *Balk,* 198 U.S. 215. But, the analogy is inapplicable in our case because, in bankruptcy proceedings, the filing of the petition and the adjudication is deemed notice to the world, except where the Act requires more specific notice.

Affirmed.

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[12] We express no opinion as to whether the bank will, in fact, have to pay any part of these checks. As noted above, the order ran against the bank and Eureka Fisheries jointly, and Eureka Fisheries has paid the trustee the full amount of the checks in question. The rights as between the bank and Eureka Fisheries have yet to be determined.

[fol. 132]

IN THE UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

No. 19,776

BANK OF MARIN, Appellant,

vs.

JOHN M. ENGLAND, Trustee in Bankruptcy in the matter of Marin Seafoods, Inc., and Eureka Fisheries, Inc., Appellee.

Appeal from the United States District Court for the Northern District of California, Southern Division.

JUDGMENT—October 28, 1965

This Cause came on to be heard on the Transcript of the Record from the United States District Court for the Northern District of California, Southern Division and was duly submitted.

On Consideration Whereof, It is now here ordered and adjudged by this Court, that the judgment of the said District Court in this Cause be, and hereby is affirmed.

Filed and entered October 28, 1965.

[fol. 133] Clerk's Certificate to foregoing transcript (omitted in printing).

[fol. 134]

SUPREME COURT OF THE UNITED STATES

No. 950—October Term, 1965

BANK OF MARIN, Petitioner,

v.

JOHN M. ENGLAND, Trustee in Bankruptcy

ORDER ALLOWING CERTIORARI—February 21, 1966

The petition herein for a writ of certiorari to the United States Court of Appeals for the Ninth Circuit is granted, and the case is placed on the summary calendar.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

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In the Supreme Court
OF THE
United States

OCTOBER TERM, 1966

No. ~~950~~ 63

BANK OF MARIN,
Petitioner,
vs.
JOHN M. ENGLAND, Trustee
in Bankruptcy,
Respondent.

PETITION FOR A WRIT OF CERTIORARI
to the United States Court of Appeals
for the Ninth Circuit

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In the Supreme Court
OF THE
United States

OCTOBER TERM, 1966

No.

BANK OF MARIN,
Petitioner,
vs.
JOHN M. ENGLAND, Trustee in Bankruptcy,
Respondent.

PETITION FOR A WRIT OF CERTIORARI
to the United States Court of Appeals
for the Ninth Circuit

Petitioner, Bank of Marin, prays that a Writ of Certiorari issue to review the judgment of the United States Court of Appeals for the Ninth Circuit entered in the above entitled case on October 28, 1965.

OPINIONS BELOW

The memorandum opinion of the District Court for the Northern District of California (R 55-56) incor-

porating the opinion of the Referee in Bankruptcy is unreported, as is the opinion of the Referee (R 112-113; Appendix A pp. xvii-xix). The opinion of the Court of Appeals for the Ninth Circuit is reported at 352 F. 2d 186 (1965). (Appendix A pp. i-xv.)

JURISDICTION

The judgment of the Court of Appeals for the Ninth Circuit was made and entered on October 28, 1965. (R. 121; Appendix A p. xvi.) The jurisdiction of this Court is conferred by 11 U.S.C. 47(c) and 28 U.S.C. 1254(1).

QUESTION PRESENTED

Whether a Bank which honored checks of a depositor after the depositor had filed a voluntary Petition in Bankruptcy is liable to the Trustee in Bankruptcy for the amount of the checks paid, where the Bank had no notice whatsoever of the bankruptcy proceedings.

STATUTES, FEDERAL RULES AND REGULATIONS INVOLVED

The applicable portions of the Fifth Amendment of the United States Constitution, Bankruptcy Act Section 18(f) (11 U.S.C. 41(f)) and Bankruptcy Act Section 70 (11 U.S.C. 110) are set forth in Appendix B pp. xx-xxi.

STATEMENT OF THE CASE

The relevant facts are not in dispute. (R 121.) Between August 27, 1963 and September 17, 1963, Marin Seafoods, Inc., drew and delivered five checks in favor of Eureka Fisheries, Inc. on its commercial account with the petitioner Bank of Marin, San Rafael, California. The total amount of the checks was $2,312.82. (R 121.)

On September 26, 1963, before the checks were presented to the Bank of Marin for payment, Marin Seafoods, Inc. filed a voluntary Petition in Bankruptcy in the United States District Court for the Northern District of California, Southern Division, located at San Francisco, California. (R 121.) John M. England was appointed as Receiver and acted as such until October 20, 1963, at which time he became Trustee for the Bankrupt. (R 122.)

On October 2, 1963, the checks which Marin Seafoods, Inc. had drawn and delivered to Eureka Fisheries, Inc. prior to the filing of the Petition in Bankruptcy were duly presented to the Bank of Marin by Eureka Fisheries, Inc. for payment. (R 122.) There were sufficient funds on deposit and the Bank of Marin honored the checks. At the time the Bank of Marin paid the checks it had received no notice, and had not otherwise obtained knowledge of the filing of the voluntary Petition in Bankruptcy by Marin Seafoods, Inc. (R 122.) The Bank of Marin was not informed of the pending bankruptcy proceedings until October 3, 1963, when it received a letter dated Octo-

ber 2, 1963 from the Receiver. (R 122.) This was one day after the Bank had honored the five checks.

The Trustee thereupon applied to the Referee for a Turnover Order pursuant to Section 2(a) of the Bankruptcy Act (11 U.S.C. 11(a)) seeking to require the Bank to pay over to the Trustee a sum of money equivalent to the sum it paid Eureka Fisheries, Inc. on October 2, 1963. (R 122.) In the alternative, the Trustee sought relief against Eureka Fisheries, Inc. After the ensuing Order To Show Cause proceeding, the Referee held that the Bank of Marin and Eureka Fisheries, Inc. were jointly liable to the Trustee for the sum of $2,312.82, the amount paid by the Bank of Marin to Eureka Fisheries, Inc. (R 122.) Subsequently, Eureka Fisheries, Inc. paid the total amount of $2,312.82 to the Trustee and then filed with the Bankruptcy Court, and served upon the Bank, a notice of payment and demand for contribution as required by California Code of Civil Procedure Section 709 (R 68, 69.)[1]

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[1]The applicable portions of California Code of Civil Procedure Section 709 provide:

"Party Who Pays More Than His Share May Compel Contribution. When property, liable to an execution against several persons, is sold thereon, and more than a due proportion of the judgment is satisfied out of the proceeds of the sale of the property of one of them, or one of them pays without a sale, more than his proportion, he may compel contribution from the others; . . . In such case, the person so paying or contributing is entitled to the benefit of the judgment, to enforce contribution or repayment, if, within ten days after his payment, he file with the Clerk of the Court where the judgment was rendered, notice of his payment and claim to contribution or repayment. Upon a filing of such notice, the

The Bank of Marin petitioned for a review of the Referee's Order pursuant to Section 39(c) of the Bankruptcy Act (11 U.S.C. 67(c)). (R 123.) The District Court affirmed the Referee's decision and the Bank then appealed that decision in accordance with Section 24 (11 U.S.C. 47) and Section 25 (11 U.S.C. 48) of the Bankruptcy Act. (R. 123.) The Court of Appeals for the Ninth Circuit made and entered its Judgment affirming the decision of the District Court on October 28, 1965.

The Bank has taken the position at each successive stage in these proceedings that it is not liable to a Trustee in Bankruptcy when, in good faith, and without notice of the bankruptcy proceedings, it honors the checks of a bankrupt depositor in the regular course of business after the filing of a voluntary petition. However, the Referee, the District Court and the Court of Appeals, after having considered the question, have held that the lack of notice affords no protection to the Bank of Marin.

Clerk must make an entry thereof in the margin of the docket."

Federal Rule of Civil Procedure Section 69 provides that the process to enforce a judgment, by execution or otherwise, is that applicable in the State where the District Court is held. [See: *Schram v. Spivak* (D.C.Mich. 1946) 68 F. Supp. 451, holding that the Michigan procedure similar to that set forth in California Code of Civil Procedure Section 709 was available in Federal Court.]

California Code of Civil Procedure Section 709 enables a joint judgment debtor, who pays more than his portion, to use the judgment to enforce contribution from his co-debtor by immediate execution without the necessity of further proceedings. *Tucker v. Nicholson*, 12 C. 2d 427, 84 P. 2d 1045 (1938); *Painter v. Bergland*, 31 C.A. 2d 63, 87 P. 2d 360 (1939).)

REASONS FOR GRANTING THE WRIT

(1) The Court of Appeals has decided an important question arising under the Federal Bankruptcy Act that has not been previously settled by this Honorable Court and has not been resolved by any other Court of Appeals. The only prior reported decision was rendered by a District Court in *Rosenthal v. Guaranty Bank & Trust Co.* (D.C. La. 1956), 139 F. Supp. 730, and is in direct conflict with the decision rendered by the Court of Appeals in this case.

The issue that was presented to the Court of Appeals and which is of such importance, that it should be settled by this Court involves the interpretation and application of Bankruptcy Act Section 70 (11 U.S.C. 110) in connection with Bankruptcy Act Section 18(f) (11 U.S.C. 41(f)).

The lower Court held that Bankruptcy Act Section 70(a) (11 U.S.C. 110(a)) vests the Trustee in Bankruptcy, by operation of law, with the title of the bankrupt to its bank deposits as of the date of the filing of the voluntary petition. Therefore, the Court reasoned, the Bank is liable to the Trustee for an amount equivalent to the amount of the checks it honored after the bankruptcy of its depositor, Marin Seafoods, Inc., even though it had no notice of the bankruptcy and was acting in good faith. In so doing, the Court of Appeals decided that nothing in Section 70(d) (11 U.S.C. 110(d)) of the Bankruptcy Act afforded the Bank protection, including the negotiability provision which provides as follows: ". . .

Provided, however, that nothing in this Act shall impair the negotiability of currency or negotiable instruments".

This interpretation by the Court of Appeals of Section 70(d)(5) is erroneous and unreasonable. It eliminates from the coverage afforded by the Section the party that most frequently will be involved in a negotiation, that is, the drawee Bank.[2]

It is inconceivable that Congress intended, when it enacted Section 70(d)(5), to deny protection to the Bank where the bankrupt has his deposits. The drawee Bank is the party who can most seriously be injured by a bankrupt who withdraws money from his savings account or delivers checks on his commercial account after bankruptcy and before the bank has knowledge of that fact. A reasonable interpretation of Section 70(d)(5) and the one intended by Congress is explained in *Rosenthal v. Guaranty Bank & Trust Co.* (D.C. La. 1956) 139 F. Supp. 730. There the District Court, in deciding the same question that is presented here, held that the negotiability provision of Section 70(d)(5) was designed to protect a Bank, which in good faith and without actual knowledge of

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[2]Although delivery of a check to the payee is a negotiation in many jurisdictions, a payee receiving a check so close to the moment of bankruptcy would either be a preferred creditor (Bankruptcy Act Section 60 (11 U.S.C. 96)) or a fraudulent transferee (Bankruptcy Act Section 67 (11 U.S.C. 107)) and not entitled to retain the money in any event.

the bankruptcy, honored checks drawn upon it by a bankrupt depositor.[3]

(2) The decision of the Court of Appeals applies Bankruptcy Act Section 70 (11 U.S.C. 110) and Bankruptcy Act Section 18(f) (11 U.S.C. 41(f)) in an unconstitutional manner at variance with the appli-

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[3]The Court's reasoning in *Rosenthal* is set forth in the following quotation:

"The trustee particularly directs the court's attention to subparagraph (5) of Title 11 U.S.C.A. Section 110, subdivision d, which he says plainly and expressly states that except as provided in subdivision d and in subdivision g of Section 44 (which latter subdivision relates to real estate and has no bearing here), no other transfer after the date of the bankruptcy shall be valid against the trustee, and of course, he argues, the only exceptions stated in subdivision d are that the payments must be made both before adjudication and without notice of the pending proceedings.

"This argument is not without merit and were it not for the fact that there is appended to that section the proviso 'that nothing in this title shall impair the negotiability of currency or negotiable instrument', we would be inclined to agree. Since no court decision has been called to our attention, and none have been found interpreting the meaning or purpose of this provision, the matter must be considered res integra. When the bankruptcy occurs the bank upon which the bankrupt drew a check prior to the date of the bankruptcy finds itself caught in the intermeshing of two highly complicated systems of law. Traditionally, it is the primary function of the Bankruptcy Act to protect the creditors, to marshall the assets, and to distribute them among creditors equitably and ratably in accordance with their respective rights and interests. Negotiability tries to give the bank the maximum assurance that it will be able to cash the check without any defenses being interposed. An expansion of bankruptcy in some senses indisputably hinders the flow of commercial paper. In the absence of any prior interpretation, we agree with counsel for defendants that one of the purposes of the 'negotiability' provision in the Bankruptcy Act was to protect a bank in a case of this kind, if the bank was in good faith and had no 'actual knowledge' of the pending bankruptcy." (*Rosenthal v. Guaranty Bank & Trust Co.* (D.C.La. 1956) 139 F. Supp. 730 at p. 734.)

cable decisions of this Court relating to the necessity of notice prior to imposing liability upon a party.

The due process clause of the Fifth Amendment forbids imposing liability unless reasonable notice of the proceeding is given. *Mullane v. Central Hanover Bank & Trust Co.,* 339 U.S. 306, 94 L. ed. 865, 70 S. Ct. 652 (1949); *Lambert v. California,* 355 U.S. 225, 2 L. ed. 2d 228, 78 S. Ct. 240 (1957); *Walker v. Hutchinson,* 352 U.S. 112, 1 L. ed. 2d 178, 77 S.Ct. 200 (1950). The due process clause also prohibits imposing liability where to do so would require the payment of a single debt twice. *Western Union Telegraph Co. v. Pennsylvania,* 368 U.S. 71, 7 L. ed. 2d 139, 82 S. Ct. 199 (1961); *Huron Holding Corp. v. Lincoln Mine Operating Co.,* 312 U.S. 183, 85 L. ed. 725, 61 S. Ct. 513 (1941).

The lower Court's decision is clearly in conflict with the broad principles set forth in *Mullane v. Central Hanover Bank & Trust Co.,* supra, regarding the necessity of adequate notice. This Court held in *Mullane* that due process demands that the deprivation of property by adjudication be preceded by notice and an opportunity for hearing. Adequate notice was defined as being that which is reasonably calculated under all the circumstances to apprise the interested parties of the action and to afford them an opportunity to present their objections. The Court of Appeals concedes that no notice was given the Bank. It further states that the Bankruptcy Act does not require that notice precede imposing liability upon the Bank. Such a decision is patently

inconsistent with the well established principles set forth by this Court.

The lower Court erroneously attempted to distinguish the notice requirements of due process as set forth in *Mullane* by taking the position that all that is required is that the Bank have notice of the hearing on the Turnover Order as opposed to notice of the adjudication of bankruptcy. Such a distinction is without merit. The Bank's rights and duties were fixed at the time of the adjudication of bankruptcy of which it had no notice. This was the point in time where the Bank's obligation was shifted from the bankrupt to the Trustee. It is this proceeding that is the relevant one and the one of which the Bank is entitled to receive reasonable notice before its rights can be affected.

The Court of Appeals avoided the second due process issue presented by the Bank. This Court has on numerous occasions stated that there is a strong constitutional policy against requiring double payment of the same debt. (See: *Western Union v. Pennsylvania,* 368 U.S. 71, 7 L. ed. 2d 139, 82 S. Ct. 199 (1961); *Huron Holding Corp. v. Lincoln Mine Operating Co.,* 312 U.S. 183, 85 L. ed. 725, 61 S. Ct. 513 (1941)). The lower Court's decision is clearly contrary to the expressions of this Court in that regard.

It is conceded that the relationship of a Bank to a depositor is that of a debtor and creditor and that the Bank is obligated to discharge its indebtedness by honoring checks drawn by its depositor. Failure to

honor such checks results in liability to the depositor. (See: *Weaver v. Bank of America,* 59 C. 2d 428, 380 P. 2d 644 (1963); *Reeves v. First National Bank,* 20 Cal. App. 508, 129 Pac. 800 (1912); *Allen v. Bank of America,* 58 Cal. App. 2d 124, 136 P. 2d 345 (1943)). The Bank in honoring the checks was properly discharging its indebtedness in accordance with its obligation to its depositor. The decision of the Court of Appeals now requires the Bank to satisfy its obligation again, this time to the Trustee.

The Court of Appeals disregarded the due process problem by holding that as of the moment of the filing of the petition, the Bank's duty with regard to the deposit was owed to the Trustee, not to the bankrupt, and consequently the Bank, in honoring the checks, was not satisfying an obligation. The Court of Appeals did not deal with the crucial issue involved, that is, whether the Bank's obligation could be transferred from the depositor to the Trustee without giving the Bank notice of the fact and that lacking such notice, the Bank can be held liable if it honored its depositor's checks in good faith. The basic principles established by the Supreme Court demand that the Bank be informed that it no longer is obligated to its depositor before it can be held responsible to the Trustee under such circumstances.

(3) The question presented is of great economic importance to the banking industry, whose interest is evidenced by the fact that the California Bankers Association filed an amicus curiae brief with the Court of Appeals. The decision of the lower Court

will apply to commercial and savings accounts in banks and savings and loan associations. By considering the vast number of checks that are honored and withdrawals that are made daily throughout the United States in conjunction with the substantial number of Petitions in Bankruptcy that are filed daily in every District Court, the true magnitude of the economic burden that has been placed upon banks and other depositories becomes apparent.[4]

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[4]The Court of Appeals stated that it felt that the problem before it was not of significant economic importance because of the fact that the *Rosenthal* case, *supra* (D.C.La. 1956) 139 F.Supp. 730 and this case, were the only reported decisions dealing with the particular problem. This is not a correct statement and is easily explained. Prior to the enactment of Bankruptcy Act Section 18(f) (11 U.S.C. 41(f)) in 1959, there was a time lag between the time of the filing of a voluntary petition and the adjudication of bankruptcy. During this period banks were protected by Bankruptcy Act Section 70(d) (11 U.S.C. 110(d)). Section 70(d) in this regard incorporated what has been well settled case law prior to 1938, the date of the enactment of Section 70(d). (See: *Citizens National Bank v. Johnson* (6th Cir. 1923) 286 Fed. 527; *Matter of Retail Stores Delivery Corp.* (D.C. N.Y. 1935) 11 F.Supp. 658.)

Although no formal notice was given, a bank would receive notice of the proceeding prior to the actual adjudication informally from the receiver or trustee just as the Bank of Marin ultimately received notice in this proceeding. Since banks actually became aware of the bankruptcy before adjudication, and had an opportunity to protect themselves, the question presented here did not arise.

However, Bankruptcy Act Section 18(f) (11 U.S.C. 41(f)) made adjudication coincidental with the filing of a voluntary petition. With the time lag eliminated, the period during which banks received actual notice and took steps to avoid liability was removed.

The enactment of Section 18(f), which was an amendment to former Section 18(g), was intended to effect only a procedural change brought about because prior to the amendment the district Judge was required to hear all voluntary petitions and to make the adjudications or dismiss the petition. Adjudication became a matter of course since there were no issues to be presented. In order to simplify the process, adjudication was then made automatic upon the filing of a voluntary petition. (See: House Report No. 241 on H.R. 4692, 86th Congress First Session (1959) 1, 2.)

Although the Court of Appeals points out that there is virtually no feasible method by which the Bank may acquire timely notice of the bankruptcy of a depositor and protect itself, the Court of Appeals states that the burden of incurring such liability should be placed on a bank even though it is the only party to the transaction who is acting in good faith.[5] Surely, this was not the intention of Congress when it enacted Section 70 of the Bankruptcy Act (11 U.S.C. 110) nor was it intended to be the result of the amendment to Bankruptcy Act Section 18(g) (11 U.S.C. 41(g)).

CONCLUSION

For the foregoing reasons, it is respectfully submitted that the Petition For A Writ Of Certiorari be granted.

Dated, San Rafael, California,
January 19, 1966.

CARLOS R. FREITAS,
FREITAS, ALLEN, MCCARTHY & BETTINI,
Attorneys for Petitioner.

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[5]A bankrupt is obviously aware of the ramifications of his act. The transfer to the payee would either be avoidable preference (Bankruptcy Act Section 60 (11 U.S.C. 96)) or a fraudulent transfer (Bankruptcy Act Section 67 (11 U.S.C. 107)).

(Appendices A and B Follow)

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Appendix A

United States Court of Appeals
for the Ninth Circuit

Bank of Marin, Appellant, vs. John M. England, Trustee in Bankruptcy in the matter of Marin Seafoods, Inc. and Eureka Fisheries, Inc., Appellee.	No. 19,776

[October 28, 1965]

Appeal from the United States District Court
for the Northern District of California
Southern Division

Before: Hamley, Jertberg and Merrill, Circuit Judges

Hamley, Circuit Judge:

Bank of Marin appeals from a district court judgment affirming an order of a referee in bankruptcy holding the bank and Eureka Fisheries, Inc., jointly liable to a trustee in bankruptcy for the sum of $2,312.82. The sole question presented is whether a bank which honored checks of a depositor after the

depositor had filed a voluntary petition in bankruptcy is liable to the trustee in bankruptcy for the amount of the checks paid where the bank had no notice of the bankruptcy proceeding.

The relevant facts are not in dispute. Between August 27, 1963, and September 17, 1963, Marin Seafoods drew and delivered five checks in favor of Eureka Fisheries upon its commercial account with Bank of Marin, San Rafael, California. The total amount of the checks was $2,318.82. On September 26, 1963, before these checks had been presented to the bank for payment, Marin Seafoods filed a voluntary petition in bankruptcy. The petition was filed in the United States District Court for the Northern District of California, Southern Division. John M. England was appointed as receiver and so acted until October 20, 1963, at which time he became trustee for the bankrupt.

On the date of the filing of the petition, sums of money in excess of $3,200 were due and owing Marin Seafoods from customers for merchandise previously delivered. Beginning on the day after the filing of the petition, and continuing for several days, Marin Seafoods, through its principal officer, collected portions of these outstanding accounts receivable and deposited them in the company's commercial account at the bank. On October 2, 1963, the checks which Marin Seafoods had drawn and delivered to Eureka Fisheries prior to the filing of the petition, were duly presented to the bank by Eureka Fisheries for payment, and were paid.

At the time the bank paid these checks it had received no notice, and had not otherwise obtained knowledge of the filing of the petition in bankruptcy. The bank was not informed of the pending bankruptcy proceeding until October 3, 1963, when it received a letter, dated October 2, 1963, from the receiver. This was one day after the bank had honored the checks referred to above.

Proceeding under section 2(a) of the Bankruptcy Act (Act), 52 Stat. 842 (1938), as amended, 11 U.S.C. § 11(a) (1964), the trustee applied to the referee for a turnover order. The trustee sought to require the bank to pay over to the trustee a sum of money equivalent to the sum paid by the bank to Eureka Fisheries on October 2, 1963. In the alternative he sought relief against Eureka Fisheries. A show cause proceeding ensued, resulting in the entry of an order by the referee, supported by findings of fact and conclusions of law. The referee determined that the bank and Eureka Fisheries were jointly liable to the trustee for the sum of $2,312.82, the amount paid by the bank to Eureka Fisheries.

In so ruling, the referee held that the bank's lack of knowledge of the filing of the voluntary petition in bankruptcy by its depositor Marin Seafoods, afforded the bank no protection. Eureka Fisheries paid the total amount of $2,312.82 to the trustee and then filed with the bankruptcy court, and served upon the bank, a demand for contribution. The bank petitioned for a review of the referee's order, and on such review,

that order was affirmed. This appeal by Bank of Marin followed.

In seeking recovery of the stated amount from the bank, the trustee relied upon section 70(a) of the Act, 52 Stat. 879 (1938), as amended, 11 U.S.C. § 110(a) (1964). This section provides, in pertinent part, that, upon his appointment and qualification, a trustee in bankruptcy shall be vested "by operation of law" with the title of the bankrupt as of the date of the filing of the petition initiating a proceeding in bankruptcy, with exceptions not here material, to described kinds of property wherever located. Among the kinds of property so described, the statute includes:

> ". . . (5) property, including rights of action, which prior to the filing of the petition he [bankrupt] could by any means have transferred or which might have been levied upon and sold under judicial process against him, or otherwise seized, impounded, or sequestered: *Provided,* . . . . [not here material]."

This provision of the Act, considered by itself, would appear to support the trustee's application for a turnover order against the bank. The bank, however, contends that notwithstanding this statute, it should be held that a bank is not liable to a trustee in bankruptcy when, in good faith, and without actual knowledge of the bankruptcy proceedings, it honors the checks of a bankrupt depositor in the regular course of business after the adjudication of bankruptcy. As authority for this view, the bank cites

Rosenthal v. Guaranty Bank & Trust Co., D.C. La., 139 F. Supp. 730, stating that the holding in that case is "determinative" of this appeal.[1]

In *Rosenthal*, on facts quite similar to those of the case before us, the court held that the proviso of section 70(d)(5) of the Act, 52 Stat. 882 (1938), 11 U.S.C. § 110(d)(5), providing that nothing in the Act ". . . shall impair the negotiability of currency or negotiable instruments . . ." protects a bank in such circumstances.[2]

As indicated by the introductory words of section 70(d), all of that subsection applies only to transactions taking place during the interval, if any, between the filing of a petition in bankruptcy and the adjudication or the taking of possession by a receiver, whichever first occurs. But, in the case of voluntary petitions in bankruptcy, such as the one before us, there is no such interval, because the filing

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[1]It would perhaps have been better if the bank had referred to the *Rosenthal* case as "persuasive". In the judicial scheme of things, a district court decision which has not withstood the acid test of appellate review cannot be regarded as authoritative, much less dispositive of an appeal, but it may well be persuasive.

[2]Section 70(d)(5) reads:

"(d) After bankruptcy and either before adjudication or before a receiver takes possession of the property of the bankrupt, whichever first occurs—

. . . .

"(5) A person asserting the validity of a transfer under this subdivision shall have the burden of proof. Except as otherwise provided in this subdivision and in subdivision (g) of section 44 of this title, no transfer by or in behalf of the bankrupt after the date of bankruptcy shall be valid against the trustee: *Provided, however,* That nothing in this title shall impair the negotiability of currency or negotiable instruments."

of a voluntary petition operates as an adjudication. Section 18(b) of the Act, 73 Stat. 109 (1959), 11 U.S.C. § 41(b) (1964). Therefore section 70(d)(5) of the Act, relied upon by the court in *Rosenthal*, can have no application here.[3]

Moreover, the presentation of a check to the drawee for payment, and the payment thereof, is not a negotiation of the check.[4] If it is not negotiation, an order declaring invalid the presentation and payment is not impairment of negotiation. Accordingly, the "negotiability" proviso of section 70(d)(5) has no application.[5]

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[3]Earlier cases in which banks were protected in paying checks all involved payments made after filing of the bankruptcy petition but prior to adjudication. See *Citizens' National Bank v. Johnson*, 6 Cir., 286 Fed. 527; *Matter of Retail Stores Delivery Corp.*, D.C.N.Y. 11 F.Supp. 658.

[4]See *Shammas v. Boyett*, 114 Cal.App.2d 139, 249 P.2d 880, 883; *Fidelity & Deposit Co. of Maryland v. Marion Nat'l Bank*, 116 Ind. App. 453, 64 N.E.2d 583; *Aurora State Bank v. Hayes-Eames Elevator Co.*, 88 Neb. 187, 129 N.W. 279; *First Nat'l Bank v. United States Nat'l Bank*, 100 Or. 264, 197 P. 547, 555; Seligson, *Creditors' Rights*, 32 N.Y.U.L.Rev. 708, 730-31 (1957); 4 Collier, *Bankruptcy* § 70.68 at 1502-03 n. 3 (14th ed. 1964); Britton, *Bills and Notes*, 118 (2d ed. 1961). Similarly, a drawee bank which has paid the check does not become a holder in due course. *Central Bank and Trust Co. v. General Finance Corp.*, 5 Cir., 297 F.2d 126, 128-29.

[5]It should also be noted that *Rosenthal* was decided in 1956, which was prior to the enacting of section 18(f) of the Act, making the filing of a voluntary petition in bankruptcy an automatic adjudication. However, for the purpose of applying chapters I through VII of the Act, the court in *Rosenthal* treated the approval of the petition for reorganization under chapter X as equivalent to adjudication pursuant to section 102 of the Act, 52 Stat. 883 (1938), 11 U.S.C. § 502 (1964). We therefore do not regard the fact that *Rosenthal* was decided prior to the enactment of section 18(f) as a sound basis for distinguishing that case.

We conclude that the "negotiability" proviso of section 70(d)(5) does not protect the Bank of Marin under the circumstances of this case.

The bank also contends that, in California, a trustee in bankruptcy must give a bank notice of the bankruptcy by complying with section 952 of the California Financial Code before he can hold the bank liable for honoring checks of the bankrupt.

Section 952 provides that notice of an adverse claim to bank deposits may be disregarded until the adverse claimant obtains a restraining order, injunction or other court order against the bank; without such an order the bank may honor checks drawn by the depositor or allow withdrawals by him without incurring liability to the adverse claimant. The bank contends that since the Bankruptcy Act makes no provision for notice to banks, state law should apply to fill this gap. The trustee gave no notice in this case, nor did he make any attempt to comply with section 952.

A claim of this kind, made by the trustee in bankruptcy for a bankrupt depositor, is not an "adverse claim," within the meaning of such a statute. *First National Bank of Arizona v. Butler,* 82 Ariz. 361, 313 P.2d 421. Thus, even overlooking inconsistencies between section 952 and the Bankruptcy Act,[6] the Cali-

[6]Section 70(d) of the Act removes protection from transactions where actual notice is present, while under section 952 the bank is protected even though there is actual notice if the remaining statutory steps have not been taken. The bank argues, however, that this inconsistent provision of section 952 is severable leaving "at least" a requirement of actual notice as a requisite to liability under section 952.

fornia statute does not undermine the district court order under review.

The bank further argues that a court of bankruptcy is governed by equitable principles and, applying those principles to this case, must protect the bank from incurring liability for honoring checks of a depositor where it had no notice of the bankruptcy of the depositor.

Under the trustee's theory of the case the bank must, in order to avoid liability, keep itself informed of the possibility of bankruptcy proceedings involving a depositor. According to the bank, this will require it to keep advised momentarily of bankruptcy filings. This burden is enhanced by the fact that filing in any district court in the United States will have the same effect. The steps demanded for protection are cited as impractical and otherwise burdensome.

The bank's dilemma is real since it is under a duty to depositors to honor checks which are validly drawn; at the same time there is always the possibility that the depositor, without the knowledge of the bank, has become the subject of bankruptcy proceedings. The hardship to the bank of keeping itself apprised of developments in the bankruptcy court is contrasted with the relatively light burden that a notice requirement would place upon the trustee. The trustee or receiver, upon filing, is informed of the bankrupt's accounts and deposits; and notification by him to the bank would be relatively simple.

The trustee, however, takes the position that there would be no great hardship resulting to banks from

a ruling imposing liability in this case. It is argued that banks have a vital interest in the credit position of depositors and that banks are well equipped to evaluate, interpret and discover factors affecting the financial well-being of depositors. The trustee cites the reviewing of local legal publications as a method of keeping abreast of bankruptcies. Also the trustee feels that keeping posted outside the immediate area would not be an insurmountable burden. In addition, it is argued that the bank has assumed this risk of doing business and can easily pass the cost of surveillance on to its customers.

Upon considering the respective arguments, we think the bank makes out a strong case for hardship and impracticability insofar as the timely discovery of bankruptcy proceedings involving depositors is concerned. We are not as certain that the problem is one which threatens great and unprotectible financial liability. The fact that our case, and *Rosenthal,* appear to be the only reported cases dealing with this particular problem is some indication that it is not one which will frequently confront banks. Moreover, it would seem that the risk, such as it is, may ordinarily be taken into account as a cost of the business and financed as such.

It is true that courts of bankruptcy exercise certain equity powers.[7] But there is no room for equitable relief of a kind which is expressly foreclosed by the

[7]Section 2(a) of the Act, 52 Stat. 842 (1938), as amended, 11 U.S.C. § 11(a); *Pepper v. Litton,* 308 U.S. 295; *Local Loan Co. v. Hunt,* 292 U.S. 234.

Act. Section 70(d)(5), quoted in note 2, above, specifically provides that "Except as otherwise provided in this subdivision and in subdivision (g) of section 44 of this title [section 21(g) of the Act] . . ." no transfer by or in behalf of the bankrupt after the date of bankruptcy shall be valid against the trustee.[8] Neither subdivision (d) of section 70, nor subdivision (g) of section 21, authorize transfers of the kind involved in this case. Equitable relief which would, as against the trustee, validate the bank's transfer to Eureka Fisheries, would thus run counter to section 70 (d)(g), and is necessarily precluded.

The California Bankers Association, appearing in this court as *amicus curiae*, joins the bank in all of the contentions discussed above. It also presents the additional argument that the failure of the trustee to revoke the bankrupt's order for the payment of funds on deposit with the Bank of Marin bars the trustee from recovery against the bank.

The gist of this argument is as follows: (1) under section 70(a)(5) of the Act, a trustee in bankruptcy succeeds only to such rights as the bankrupt possessed at the time of the bankruptcy petition, and is subject to all defenses and equities which might have been asserted against the bankrupt but for the filing of that petition; (2) in California an ordinary depositor does not have title to any specific funds deposited in a bank, the relationship of bank and depositor, founded upon contract, being that of debtor

[8]The "negotiability" proviso to this subsection has already been discussed.

and creditor; (3) under that contract, a bank has both the right and duty to honor checks of its depositors properly drawn and duly presented, unless the depositor provides the bank with notice of the revocation of his order for payment prior to the time his checks are accepted by the bank; (4) absent the giving of a timely "stop payment" order such payment operates to discharge the bank's obligation, and the depositor has no right to recover the amounts paid; and (5) under the premise set forth at the outset, the trustee is subject to the same defense.

The bankruptcy of a drawer operates as a revocation of the drawee's authority.[9] Such revocation is not dependent upon or subject to notice to the drawee, since the trustee is immediately vested with the title of the bankrupt by operation of law. The parties to a depositor's contract with a bank are chargeable with knowing this when they enter into the contract. These circumstances constitute an implied exception to the contractual obligation of the bank to honor checks unless and until a "stop payment" notice is received. The asserted bank defense based upon lack of a "stop payment" notice is therefore not available against a trustee in bankruptcy in the case of the bankruptcy of the drawer.

Finally, both the bank and *amicus curiae* contend that the district court order under review deprives the bank of due process of law as guaranteed by the Fifth

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[9] *Harrison State Bank v. First National Bank*, 116 Neb. 456, 218 N.W. 92; *Guthrie Nat'l Bank v. Gill*, 6 Okla. 560, 54 Pac. 434; Brady, *Bank Checks*, 25 (3rd ed. 1962).

Amendment. Two aspects of this Constitutional argument are presented, the first being that the due process clause forbids imposing liability upon a bank unless it has received reasonable notice of the bankruptcy proceeding.

In support of this view, *Mullane v. Central Hanover Bank & Trust Co.*, 339 U.S. 306, and several other decisions are cited. In *Mullane,* the question involved was whether adequate notice was given to a person of litigation wherein his rights were being litigated. Prior to the turnover proceedings, however, the rights of the Bank of Marin were not being adjudicated in the bankruptcy proceedings before us. Up to then, the rights of the bank were not affected by any order entered by the referee; the property of the bankrupt was vested in the trustee by operation of law. The rule as to notice set forth in *Mullane* and similar cases, is therefore inapplicable here.

In *Lambert v. California,* 355 U.S. 225, also cited by the bank, the Court held a statute unconstitutional which imposed criminal liability not for an affirmative act, but for the failure of a convicted felon to register despite lack of notice of the requirement. Since the basis for the bank's liability to the trustee cannot be equated with the violation of a criminal statute, *Lambert* is not in point.

The bank also places reliance upon *Hanover Nat'l Bank v. Moyses,* 186 U.S. 181. There, a creditor asserted that he had not been adequately notified of the filing and adjudication of a voluntary bankruptcy. But, as in *Mullane* and most of the other decisions

cited by the bank, the rights of the creditor in *Moyses* were being adjudicated in the bankruptcy proceeding.

We do not believe that *Moyses* should be extended past its holding that the creditors of a bankrupt are entitled to reasonable notice of the bankruptcy proceedings.[10] The filing of a bankruptcy petition has long been regarded as a *caveat* to all the world. *Mueller v. Nugent,* 184 U.S. 1, 14. Likewise, adjudication has been held to be notice to the world, thus invalidating transactions involving the debtor's property occurring after adjudication. *J.S. & J.F. Sterling, Inc. v. Birkhahn,* 3 Cir., 30 F.2d 492, 495; 4 Collier, *Bankruptcy,* § 70.66 at 1498 (14th ed. 1964).

Congress may not proceed in complete disregard of the property rights of those dealing in good faith with bankrupts. It may, however, enact legislation balancing bankruptcy objectives with the interests of those dealing in good faith with a bankrupt. Section 70(d) of the Act, we believe, demonstrates that Congress has, in this balancing process, taken into account the latter interests and has accommodated them to the extent deemed feasible having in view the desirability of speedy, economical and effective bankruptcy administration.[11]

In our opinion, the order under discussion does not offend the due process clause, insofar as notice to the bank is concerned.

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[10]In *Moyses* it was held that the creditor had received sufficient notice.

[11]See *Lake v. New York Life Insurance Co.,* 4 Cir., 218 F.2d 394, 397-99; 4 Collier, *Bankruptcy,* §§ 70.66, 70.67, pages 1494-1501 (14th ed. 1964), commenting on the legislative history of section 70(d).

This brings us to the second facet of the Constitutional argument presented by the bank and *amicus curiae*. This is the contention that the due process clause prohibits imposing liability upon the bank because to do so would require the bank to pay a single debt twice. There is a strong Constitutional policy against requiring the double payment of the same debt. See *Western Union Telegraph Co. v. Pennsylvania*, 368 U.S. 71.

The argument for the bank is premised upon these propositions: the relationship of a bank to its depositor is that of debtor and creditor; the bank is obligated to discharge its indebtedness by honoring checks drawn by depositors; and failure to honor such checks results in liability to the depositor. These propositions are not challenged by the trustee for they are well established. Next the bank argues that in honoring the checks drawn by the bankrupt, it discharged its indebtedness in accordance with its obligation to its depositor. From this, the conclusion is drawn that to require a second payment now to the trustee is a violation of the Fifth Amendment.

As we have already seen, at the time the checks were honored, title to the deposits was vested in the trustee by virtue of section 70(a). From the moment of filing the petition, the bank's duty with regard to the deposits was owed to the trustee, not to the bankrupt and not to the payee of the checks. We have already held that, in legal contemplation, the filing was sufficient notice to those subsequently dealing with the bankrupt's assets. Accordingly, and regardless of

actual notice, the bank's obligation to honor the checks disappeared before it paid them. Therefore, in paying the checks when presented by Eureka Fisheries, the bank was not paying a debt for which it was obligated. It follows that if as a result of this judgment the bank pays any part of the checks, it will not be paying the same debt twice.[12]

The bank characterizes its position as analogous to a garnishee who has paid his creditor without notice of garnishment. A garnishee is not liable to the garnishor in such circumstances. *Harris v. Balk,* 198 U.S. 215. But, the analogy is inapplicable in our case because, in bankruptcy proceedings, the filing of the petition and the adjudication is deemed notice to the world, except where the Act requires more specific notice.

Affirmed.

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[12]We express no opinion as to whether the bank will, in fact, have to pay any part of these checks. As noted above, the order ran against the bank and Eureka Fisheries jointly, and Eureka Fisheries has paid the trustee the full amount of the checks in question. The rights as between the bank and Eureka Fisheries have yet to be determined.

United States Court of Appeals
for the Ninth Circuit

No. 19,776

Bank of Marin,
Appellant,
vs.
John M. England, Trustee in Bankruptcy in the matter of Marin Seafoods, Inc., and Eureka Fisheries, Inc.,
Appellee.

Appeal from the United States District Court
for the Northern District of California,
Southern Division

JUDGMENT

This Cause came on to be heard on the Transcript of the Record from the United States District Court for the Northern District of California, Southern Division and was duly submitted.

On Consideration Whereof, It is now here ordered and adjudged by this Court, that the judgment of the said District Court in this Cause be, and hereby is affirmed.

Filed and entered October 28, 1965.

In The United States District Court
For The Northern District of California
Southern Division

In the Matter of Marin Seafoods, Inc. Bankrupt.	No. 74820 In Bankruptcy

ORDER AFFIRMING REFEREE'S ORDER

Bank of Marin has petitioned for a review of the referee's order in the above entitled action adjudging it jointly liable to the trustee for $2,312.82. Petitioner argues that because of the adverse effects on the banking industry of the referee's interpretation of the statutory bankruptcy scheme and because of possible constitutional objections a contrary construction should prevail.

After a careful review of the relevant cases and authorities and a detailed evaluation of facts alleged in the briefs filed herein, this Court has concluded that under the circumstances the referee's order was proper. The findings of fact and reasoning contained in his opinion of February 24, 1964 are hereby adopted and the judgment of March 31, 1964 is hereby affirmed.

Dated, October 26, 1964.

s/ Albert C. Wollenberg
United States District Judge

United States District Court
For The Northern District of California
Southern Division

In the Matter of Marin Seafoods, Inc. Bankrupt.	No. 74820 In Bankruptcy

OPINION FOR ORDER

Title to the property of a bankrupt vests in the trustee as of the date of the bankruptcy petition pursuant to the provisions of section 70a of the Bankruptcy Act. Certain transactions thereafter but prior to adjudication are protected by section 70d. However, the statute places "an absolute ban on all transfers not given specific protection under the act". Feldman v. Capitol Piece Dye Works, Inc. (C.A. 2, 1961) 293 F. 2d 889.

No provision contained in section 70d gives any protection to a bank which after adjudication honors the checks of the bankrupt. And the recipient of such funds after adjudication merely holds property title to which is vested in the trustee.

The bank on brief questioned the summary jurisdiction of the bankruptcy court. The point is belatedly raised. Bankruptcy Act section 2(7). In any event the facts do not show the bank ever had any claim to these funds deposited with it after adjudication of the bankrupt.

The trustee is entitled to a judgment against the Bank of Marin for $700.47 and against the Bank of Marin and Eureka Fisheries, jointly, for $2,312.82.

The trustee shall serve and lodge appropriate findings of fact, conclusions of law and order.

Dated at San Francisco, California, this 24th day of February, 1964.

Lynn J. Gillard
Referee in Bankruptcy

Appendix B

United States Constitution Amendment V—Capital Crimes; Double Jeopardy; Self-Incrimination; Due Process; Just Compensation For Property

No person shall be . . . deprived of life, liberty or property without due process of law.

11 U.S.C. 41 (Bankruptcy Act Section 18(f)) . . . The filing of a voluntary petition under chapters 1 to 7 of this title, other than a petition filed in behalf of a partnership by less than all of the partners, shall operate as an adjudication with the same force and effect as a decree of adjudication.

11 U.S.C. 110 (Bankruptcy Act Section 70)

Title to property:

(a) The trustee of the estate of a bankrupt and his successor or successors, if any, upon his or their appointment and qualification, shall in turn be vested by operation of law with the title of the bankrupt as of the date of the filing of the petition initiating a proceeding under this title, except insofar as it is to property which is held to be exempt, to all of the following kinds of property wherever located . . . property, including rights of action, which prior to the filing of the petition he could by any means have transferred or which might have been levied upon and sold under judicial process against him, or otherwise seized, impounded, or sequestered. . . .

. . .

(d) After bankruptcy and either before adjudication or before a receiver takes possession of the property of the bankrupt, whichever first occurs—

(1) A transfer of any of the property of the bankrupt, other than real estate, made to a person acting in good faith shall be valid against the trustee if made for a present fair equivalent value or, if not made for a present fair equivalent value, then to the extent of the present consideration actually paid therefor, for which amount the transferee shall have a lien upon the property so transferred;

(2) A person indebted to the bankrupt or holding property of the bankrupt may, if acting in good faith, pay such indebtedness or deliver such property, or any part thereof, to the bankrupt or upon his order, with the same effect as if the bankruptcy were not pending;

(3) A person having actual knowledge of such pending bankruptcy shall be deemed not to act in good faith unless he has reasonable cause to believe that the petition in bankruptcy is not well founded;

(4) The provisions of paragraphs (1) and (2) of this subdivision shall not apply where a receiver or trustee appointed by a United States or State court is in possession of all or the greater portion of the non-exempt property of the bankrupt;

(5) A person asserting the validity of a transfer under this subdivision shall have the burden of proof. Except as otherwise provided in this subdivision and in subdivision g of section 44 of this title, no transfer by or in behalf of the bankrupt after the date of bankruptcy shall be valid against the trustee: *Provided, however,* That nothing in this title shall impair the negotiability of currency or negotiable instruments.

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In the Supreme Court
OF THE
United States

OCTOBER TERM, 1965

No. 63

BANK OF MARIN, *Petitioner,*

vs.

JOHN M. ENGLAND, Trustee in Bankruptcy, *Respondent.*

On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

BRIEF FOR THE PETITIONER

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In the Supreme Court
OF THE
United States

OCTOBER TERM, 1965

No. 950

BANK OF MARIN,
Petitioner,
vs.
JOHN M. ENGLAND, Trustee in Bankruptcy,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

BRIEF FOR THE PETITIONER

OPINIONS BELOW

The memorandum opinion of the District Court for the Northern District of California, Southern Division (R99-100) and the opinion of the referee in bankruptcy (R42-43) are unreported. The opinion of the Court of Appeals for the Ninth Circuit is reported at 352 F. 2d 186 (1965).

JURISDICTION

The judgment of the Court of Appeals for the Ninth Circuit was made and entered on October 28, 1965. The Petition for Writ of Certiorari was filed on January 26, 1966, and granted on February 21, 1966. The jurisdiction of this Court is conferred by Bankruptcy Act section 24(c), 66 Stat. 423 (1952), 11 U.S.C. 47(c); and 28 U.S.C. 1254(1).

STATUTES, FEDERAL RULES AND REGULATIONS INVOLVED

The applicable portions of the fifth amendment of the United States Constitution; Bankruptcy Act section 18(f), 73 Stat. 109 (1959), 11 U.S.C. 41; Bankruptcy Act section 70a, 52 Stat. 879 (1938) as amended, 11 U.S.C. 110(a); and Bankruptcy Act section 70d, 52 Stat. 881 (1938), 11 U.S.C. 110(d) are set forth in the appendix.

QUESTION PRESENTED

Is a bank which honored checks of a depositor after the depositor had filed a voluntary petition in bankruptcy, where the bank had no notice whatsoever of the bankruptcy proceeding, liable to the trustee in bankruptcy for the amount of the checks paid?

STATEMENT OF THE CASE

The facts are not in dispute. Between August 27, 1963, and September 17, 1963, Marin Seafoods, Inc. drew and delivered five checks, totaling $2,312.82, in favor of Eureka Fisheries, Inc. on its commercial account with the petitioner Bank of Marin, San Rafael, California. (R46.)

On September 26, 1963, before the checks were presented to the Bank of Marin for payment, Marin Seafoods filed a voluntary petition in bankruptcy in the United States District Court for the Northern District of California, Southern Division, San Francisco, California. (R44.) John M. England was appointed receiver on September 30, 1963, and acted as such until October 20, 1963, at which time he became trustee for the bankrupt. (R45.)

On October 2, 1963, the checks which Marin Seafoods had drawn and delivered to Eureka Fisheries prior to the filing of the petition in bankruptcy were duly presented for payment by Eureka Fisheries to the Bank of Marin. (R46.) Sufficient funds were on deposit and the bank in good faith honored the checks. (R8.) At the time the bank paid the checks it had received no notice, and had not otherwise obtained knowledge of the filing of the voluntary petition in bankruptcy by Marin Seafoods. (R47.) The Bank of Marin was not informed of the pending bankruptcy proceedings until the next day, October 3, 1963, when it received a letter dated October 2, 1963, from the receiver. (R46, 47.)

On November 27, 1963, the trustee applied to the referee for a turnover order pursuant to section 2(a) of the Bankruptcy Act, 52 Stat. 842 (1938), 11 U.S.C. 11(a), seeking to require the bank to pay over to the trustee a sum of money equivalent to the sum it paid Eureka Fisheries on October 2, 1963. (R1-3.) In the alternative, the trustee sought the same relief against Eureka Fisheries. Immediately, an order to show cause was issued by the referee ordering the Bank of Marin and Eureka Fisheries to show why the relief prayed for by the trustee should not be granted. (R3-4.)

After the hearing on the order to show cause, the referee held that the Bank of Marin and Eureka Fisheries were jointly liable to the trustee for the sum of $2,312.82, the amount paid by the Bank of Marin to Eureka Fisheries. (R47, 48.) Subsequently, Eureka Fisheries paid the total amount of $2,312.82 to the trustee and filed with the bankruptcy court, and served upon the bank, a notice of payment and demand for contribution pursuant to California Code of Civil Procedure section 709, thereby entitling Eureka Fisheries to the remedy of execution to recover from the bank one-half the amount Eureka Fisheries paid on the joint judgment.[1] (R54, 55.)

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[1]California Code of Civil Procedure section 709 provides:
"*Party Who Pays More Than His Share May Compel Contribution.* When property, liable to an execution against several persons, is sold thereon, and more than a due proportion of the judgment is satisfied out of the proceeds of the sale of the property of one of them, or one of them pays, without a sale, more than his proportion, he may compel contribution from the others; . . . In such case, the person so paying or contributing is entitled to the benefits of the judgment, to enforce contribution or repayment, if, within ten days after

The Bank of Marin petitioned for review of the referee's order pursuant to section 39(c) of the Bankruptcy Act, 74 Stat. 528 (1960), 11 U.S.C. 67(c). (R50, 51.) The District Court affirmed the referee's decision and the bank then appealed that decision in accordance with section 24, (66 Stat. 423 (1952), 11 U.S.C. 47) and section 25, (66 Stat. 424 (1952), 11 U.S.C. 48) of the Bankruptcy Act. (R99-105.) The Court of Appeals for the Ninth Circuit made and entered its judgment affirming the decision of the District Court on October 28, 1965. (R105-117.)

The bank has taken the position at each successive stage of these proceedings that it is not liable to a trustee in bankruptcy when, in good faith, and without notice of the bankruptcy proceedings, it honors the checks of a bankrupt depositor in the regular course of business after the filing of a voluntary petition. However, the referee, the District Court and the Court of Appeals, after having considered the question, have held that the lack of notice and the fact that the payments were made in good faith afford no protection to the Bank of Marin. (R47, 99, 100, 105-116.)

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payment, he files with the clerk of the court where the judgment was rendered, notice of his payment and claim to contribution or repayment. Upon a filing of such notice, the clerk must make an entry thereof in the margin of the docket."

This section enables a joint judgment debtor, who pays more than his portion of the judgment, to use the judgment to enforce contribution from his co-debtor by immediate execution without the necessity of further proceedings. *Tucker v. Nicholson*, 12 C. 2d 427, 84 P. 2d 1045 (1938); *Painter v. Bergland*, 31 Cal. App. 2d 63, 87 P. 2d 360 (1939); *McIntosh v. Funge*, 128 Cal. App. 70, 16 P. 2d 1006 (1932). This procedure is applicable in the federal courts. Federal Rules of Civil Procedure section 69. *Schram v. Spivak* (D. C. E. D. Mich. 1946) 68 F. Supp. 451.

SUMMARY OF ARGUMENT

I

The decision of the Court of Appeals, holding that sections 70a and 70d of the Bankruptcy Act impose liability upon a bank which, after the filing of a voluntary petition in bankruptcy by a depositor, honors checks of the depositor in good faith without notice of the bankruptcy, renders those sections violative of the due process clause of the fifth amendment of the United States Constitution.

Due process requires that a bank be given reasonable notice of the bankruptcy of one of its depositors before it can be held responsible for honoring checks of that depositor in good faith. *Mullane v. Central Hanover Bank & Trust Co.*, 339 U.S. 306 (1949); *New York v. New York N.H. & H.R. Co.*, 344 U.S. 293 (1953).

The relationship between a bank and its depositor is that of debtor and creditor giving rise to an obligation on the part of the bank to discharge its indebtedness by honoring such checks as its depositor may draw upon it. *New York County Nat. Bank v. Massey*, 192 U.S. 138 (1903). By holding that the Bank of Marin must pay to the trustee of its bankrupt depositor, Marin Seafoods, a sum equivalent to the sum that it paid in honoring the checks of Marin Seafoods, the Court of Appeals is compelling the bank to satisfy the same debt twice, thereby violating the Constitutional prohibition against forcing a person to pay the same obligation more than once. *Western Union Telegraph Co. v. Pennsylvania*, 368 U.S. 71 (1961).

II

Prior to 1938, there was no provision in the Bankruptcy Act dealing with the protection of good faith transfers of the bankrupt's property after bankruptcy. However, a considerable body of law evolved, based upon fundamental concepts of equity and justice, which protected innocent parties who dealt bona fides with the bankrupt's property. It was well established that banks which honored checks of a bankrupt depositor after bankruptcy in good faith without notice of the bankruptcy were protected in such payment.

In 1938, section 70d was added to the Bankruptcy Act as a part of the Chandler Amendment. Section 70d set forth in the act for the first time specific restrictions upon good faith transfers of the bankrupt's property after bankruptcy. The only transfers that were protected were those occurring between the time of the filing of the petition and adjudication or before a receiver took possession of the bankrupt's property.

In 1959, Bankruptcy Act section 18g was amended (renumbered as section 18f) to make adjudication automatic upon the filing of a voluntary petition. The amendment eliminated section 70d from application to voluntary bankruptcies by removing the interval during which that section was effective. Consequently, there is no longer any provision in the Bankruptcy Act limiting those situations where protection will be afforded good faith transfers of the bankrupt's property after the filing of a voluntary petition. The problem of determining which transactions are to be protected is again left up to courts which are free to

apply well established equitable principles to protect the Bank of Marin.

By relieving the Bank of Marin of liability, due process can be accorded the bank and the constitutional limitations of the Court of Appeals' interpretation of sections 70a and 70d of the Bankruptcy Act can be avoided.

III

Section 70d(5) of the Bankruptcy Act provides in part that ". . . nothing in this title shall impair the negotiability of currency or negotiable instruments". The broad language of that proviso protects transfers of negotiable instruments occurring before and after adjudication if the imposition of liability upon any party to the transaction would impair the negotiability of the instrument.

To impose liability upon a drawee bank honoring checks of a bankrupt depositor in good faith without notice of the bankruptcy, impairs the negotiability of the checks. The only means by which a bank could avoid the consequences of the Court of Appeals' decision would be to delay acceptance of a check until such time as the bank completed the impossible task of ascertaining whether the depositor had filed a petition in bankruptcy in any district in the country. This would not only violate the bank's legal obligation to its depositor to honor the checks upon presentment, but would destroy the freedom with which checks flow in the commercial world and would limit their usefulness as a substitute for money.

ARGUMENT

I

THE DECISION OF THE COURT OF APPEALS, HOLDING THE BANK LIABLE FOR HONORING CHECKS OF A DEPOSITOR IN GOOD FAITH AFTER THE DEPOSITOR FILED A VOLUNTARY PETITION IN BANKRUPTCY WHERE THE BANK HAD NOT BEEN GIVEN NOTICE, AND HAD NOT OTHERWISE OBTAINED KNOWLEDGE OF THE BANKRUPTCY, APPLIES PORTIONS OF SECTIONS 70a AND 70d OF THE BANKRUPTCY ACT IN SUCH A MANNER THAT THEY VIOLATE THE DUE PROCESS CLAUSE OF THE FIFTH AMENDMENT OF THE CONSTITUTION.

A. Due process requires that the bank be given notice of the bankruptcy of its depositor before it can be held liable for honoring checks of the depositor after bankruptcy.

Prior to the intervention of bankruptcy, the relationship between the Bank of Marin and its depositor, Marin Seafoods, was that of debtor and creditor, giving rise to an obligation on the part of the bank to discharge its indebtedness by honoring such checks as its depositor drew upon it. *New York County Nat. Bank v. Massey,* 192 U.S. 138 (1903); *Union Tool v. Farmers, etc. National Bank,* 192 Cal. 40, 218 Pac. 424 (1923); *Glassell Development Co. v. Citizens National Bank,* 191 Cal. 375, 216 Pac. 1012 (1923).

When Marin Seafoods' checks were duly presented for payment on October 2nd, there were sufficient funds on deposit to its credit with the Bank of Marin and the bank in good faith proceeded to pay the checks (R8, 46, 47.) The Court of Appeals, nevertheless, has held that the Bank of Marin is liable to the trustee in bankruptcy for an amount equivalent to the sum it paid in honoring the checks.

The decision of the Court of Appeals turned upon its interpretation of the effect of Bankruptcy Act section 70a in conjunction with Bankruptcy Act section 70d. It held that section 70a vested the trustee in bankruptcy, by operation of law, with the title of the bankrupt to its bank deposits as of the date of the filing of the voluntary petition. Therefore, the Court reasoned, the Bank of Marin must be liable to the trustee for the sums it paid in honoring the checks after the bankruptcy of its depositor, Marin Seafoods, even though it had no notice of the bankruptcy and was acting in good faith. In so doing, the Court decided that the only transactions that are protected after bankruptcy are those coming within the purview of Bankruptcy Act section 70d and that nothing in that section afforded the bank relief.

Although it was conceded by the Court of Appeals that no notice was given to the bank and that it had not otherwise acquired knowledge of the bankruptcy, the Court imposed liability upon the bank. (R106.) It stated that the bank was not entitled to any notice beyond the caveat that accompanies the filing of a voluntary petition. It is the position of the petitioner, Bank of Marin, that such an application of Bankruptcy Act would render sections 70a and 70d[2] violative of the due process clause of the Fifth Amendment of the United States Constitution.

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[2]The applicable portions of Bankruptcy Act sections 70a, 52 Stat. 879 (1938) as amended, 11 U.S.C. 110(a), and 70d, 52 Stat. 881 (1938), 11 U.S.C. 110(d), are set forth in the Appendix.

The exercise of the constitutional grant of power to Congress to legislate on the subject matter of bankruptcies (U.S. Constitution, article I, section 8, chapter 4) is limited by the due process clause of the Fifth Amendment. *Louisville Joint Stock Land Bank v. Radford,* 295 U.S. 555 (1935); *Hanover National Bank v. Moyses,* 186 U.S. 181 (1902). Congress may prescribe regulations concerning bankruptcies, but it may not dictate regulations that are so grossly unreasonable as to be incompatible with fundamental law and due process. *Hanover National Bank v. Moyses,* 186 U.S. 181 (1902); *Louisville Joint Stock Bank v. Radford,* 295 U.S. 555 (1935).

It is no longer open to question that an elementary and fundamental requirement of due process is that deprivation of property by adjudication be preceded by notice and an opportunity for hearing. *Mullane v. Central Hanover Bank & Trust Co.,* 339 U.S. 306 (1949). The principles enunciated by this Court in *Mullane v. Central Hanover Bank & Trust Co.,* 339 U.S. 306 (1949), regarding notice have been consistently followed and applied. It is necessary that reasonable notice of a condemnation action be given a landowner prior to the time his rights are affected, even though the governmental authority has the absolute right to condemn. *Walker v. City of Hutchinson,* 352 U.S. 112 (1950); *Schroeder v. City of New York,* 371 U.S. 208 (1962). Similarly, due process requires that notice of foreclosure of a tax lien be given the defaulting taxpayer upon whose real property the tax has become a lien. *Covey v. Town of Somers,* 351

U.S. 141 (1956). In a like manner, it is held that beneficiaries of a common trust fund be given notice of all proceedings which affect their interests in order to satisfy due process. *Mullane v. Central Hanover Bank & Trust Co.*, 339 U.S. 306 (1949).

More specifically, this Court held in *New York v. New York N. H. and H. R. Co.*, 344 U.S. 293 (1953), that a city having a lien upon specific real property of a railroad reorganizing under section 77 of the Bankruptcy Act must be given notice of those stages of the proceedings where its rights would be affected consistent with the requirements established in *Mullane*. The principles relied upon in the *New York v. New York N. H. and H. R. Co.* case apply with equal force to any person whose property rights will be adversely affected by bankruptcy.

Where notice is required by due process, it must be given prior to the time when property rights are disturbed. *Lambert v. California*, 355 U.S. 225 (1957).

> ". . . Notice is required before property interests are disturbed, before assessments are made, before penalties are assessed. Notice is required in a myriad of situations where a penalty or forfeiture might be suffered for mere failure to act. Recent cases illustrating the point are *Mullane v. Central Hanover Bank & Trust Co.*, 339 U.S. 306; *Covey v. Town of Somers*, 351 U.S. 141; *Walker v. Hutchinson City*, 352 U.S. 112. These cases involved only property interests in civil litigation. But the principle is equally appropriate where a person, wholly passive and unaware of any wrongdoing, is brought to the bar of justice for con-

demnation in a criminal case." (*Lambert v. California,* 355 U.S. 225 at p. 228.)

The Court of Appeals stated that the requirements of due process have been met since the Bank of Marin received notice of the hearing on the turnover order. The position of that Court in this regard is not well taken. If the Court is correct in holding that adjudication has the effect of shifting the bank's obligation to pay from its depositor to the trustee as of the date of the filing of the petition, the bank must receive reasonable notice of that event so that it may decide whether or not to honor the checks as they are presented with full knowledge of the possible consequences. Notice of any subsequent proceeding, such as the hearing on the turnover order, is obviously ineffectual to give the bank an opportunity to protect itself by refusing to honor the checks.

The type of notice that must be given in order to satisfy due process is that which is reasonably calculated, under all the circumstances, to apprise interested parties of the pending action. *Mullane v. Central Hanover Trust & Bank Co.,* 339 U.S. 306 (1949). If the act of filing a voluntary petition is notice of any kind, it is certainly not reasonably calculated to put the bank on notice of its filing. Although the filing of the petition is often considered to be caveat to the whole world, it has been stated that the caveat is not equivalent to effective notice in many situations. *Jones v. Springer,* 226 U.S. 148 (1912); *Frederick v. Fidelity Mut. Ins. Co.,* 256 U.S. 395 (1921).

The reasonableness and hence the constitutional validity of any given mode of notice is determined by balancing the certainty that the notice will reach those affected against the feasibility of giving such notice. *Mullane v. Central Hanover Trust & Bank Co.,* 339 U.S. 306 (1949). The trustee (initially the receiver) knew of the existence and the location of the Marin Seafoods deposit with the Bank of Marin. Under the circumstances it would not have been burdensome in any respect to telephone or to mail notice to the bank. As stated in *Mullane* (339 U.S. 306, 318 (1949):

> ". . . Where the names and postoffice addresses of those affected by a proceeding are at hand, the reasons disappear for resort to means less likely than the mails to apprise them of its pendency."

The trustee made much out of the argument that the bank could have discovered that one of its depositors had filed a petition in bankruptcy by searching the various legal newspapers that are independently published. However, it is a practical impossibility to accomplish such a task. While in this case the petition was filed in the adjoining county of San Francisco, to be fully protected the bank would have to keep itself advised momentarily of every bankruptcy filing in every district in the country. Moreover, the fact that the bank might have acquired knowledge is not a substitute for the failure of the trustee to fulfill the requisites of due process by providing reasonable notice. *Wuchter v. Pizzutti,* 276 U.S. 13 (1928).

B. The bank cannot be compelled to pay the same debt twice.

Due process not only requires that a person receive adequate notice prior to the time his property interests are disturbed, but it also protects a person from paying the same debt more than once. *Western Union Telegraph Co. v. Pennsylvania,* 368 U.S. 71 (1961); *Harris v. Balk,* 198 U.S. 215 (1905); *Huron Holding Corp. v. Lincoln Mine Operating Co.,* 312 U.S. 183 (1941).

The bank was obligated to discharge its indebtedness to Marin Seafoods by honoring the checks which were drawn upon it. *New York County Nat. Bank v. Massey,* 192 U.S. 138 (1903); *Glassell Development Co. v. Citizens National Bank,* 191 Cal. 375, 216 Pac. 1012 (1923). Based upon the facts that were known to the bank at the time the checks were presented for payment on October 2, the bank would have been liable for damages to its depositor had it not fulfilled this obligation. *Weaver v. Bank of America,* 59 C. 2d 428, 380 P. 2d 644 (1963). The decision of the Court of Appeals, ordering the bank to pay an equivalent sum to the trustee, compels the bank to pay the same debt twice.

The Court discounted the double payment problem by taking the position that as of the moment of the filing of the voluntary petition, the bank's duty with regard to the deposit was shifted from its depositor to the trustee, and consequently, the bank, in honoring the checks was not satisfying an obligation. The Court did not face up to the basic issue presented, that is,

can the bank's obligation to its depositor be transferred to the trustee without giving the bank notice of that fact, and that lacking such notice, can the bank be held to dual liability if it honors its depositor's checks in good faith without notice? The imposition of such a burden upon the bank violates the basic precepts of due process that have been long established by this Court. The right to notice and to protection from double payment are two of the cornerstones of due process. Lack of these cornerstones constitutes an absence of that fundamental fairness essential to the very concept of justice.

II

COURTS REPEATEDLY HAVE HELD THAT EQUITABLE PRINCIPLES APPLY UNDER THE BANKRUPTCY ACT TO PROTECT A BANK HONORING CHECKS AFTER A DEPOSITOR'S BANKRUPTCY WHEN THE BANK HAS NO NOTICE OF THE BANKRUPTCY.

A. Bankruptcy Act section 70d does not apply to voluntary bankruptcies.

The Court of Appeals held that section 70a vested the trustee with the title of the bankrupt to its deposit as of the date of the filing of the petition and that honoring a prior transfer of any portion of that deposit after bankruptcy could be valid against the trustee only if it was authorized by section 70d. Since that section makes no provision for transfers taking place after adjudication, the Court determined that any interpretation of the Act that would protect the Bank of Marin would conflict with section 70d and was therefore precluded.

However, section 70d has no application to voluntary proceedings. The introductory clause of that section which provides that: "After bankruptcy and either before adjudication or before a receiver takes possession of the property of the bankrupt, whichever first occurs—", clearly limits section 70d's application to transactions occurring during the interval between the filing of a petition and before adjudication or before the receiver takes possession of the property of the bankrupt. If there is no such interval, section 70d does not apply.

Prior to 1959, there was a lapse of time between the filing of a petition and the adjudication of bankruptcy in both voluntary and involuntary cases during which transfers falling within the purview of section 70d were protected. However, in 1959, section 18g of the Act was amended and renumbered as section 18f. Section 18f made adjudication automatic on the filing of a voluntary petition thereby eliminating the interval that previously existed. With the removal of this time period, there can be no instance where section 70d would apply in a voluntary bankruptcy since by its terms adjudication is the cutoff date.[3] The

[3]It was not the intent of Congress in enacting section 18f to effect any change in the substance of section 70d or to deny its application to a voluntary bankruptcy. Section 18f was designed to bring about a procedural change by making adjudication automatic upon the filing of a voluntary petition. Under the prior section (18g) the district judge was required to hear all voluntary petitions and to either make the adjudication or dismiss the petition. Since there were no issues to be presented, adjudication became a matter of course. By making adjudication automatic, Congress intended to remove the burden of hearing all the petitions from the district judge. (See: House Report 241 on H. R. 4692, 86 Cong. 1st Sess. (1959) 1, 2). No consideration was given

result is the complete elimination from the Bankruptcy Act of any provision dealing with the protection of bona fide transfers after the filing of a voluntary petition.

B. Prior to the enactment of section 70d, courts of bankruptcy protected banks honoring a bankrupt depositor's checks after bankruptcy in good faith without notice.

Petitioner does not contend that the Bankruptcy Act specifically provides that the bank receive notice of the filing of a petition in bankruptcy or of the adjudication of a depositor. It is clear that there is no such provision in the Act. However, it is a cardinal principle long established by this Court that a statute will be interpreted so as to avoid possible constitutional limitations. *United States v. Rumely,* 345 U.S. 41 (1952); *Wright v. Mountain Trust Bank,* 300 U.S. 440 (1936). The Bankruptcy Act can be construed so that it does not violate the due process limitations previously discussed by either implying the requirement of notice, or, by holding that its provisions do not impose liability upon a bank under the facts presented here.

Section 70d was added to the Bankruptcy Act as a part of the major revision brought about by the enactment of the Chandler Act in 1938. Prior to that time, there had been no similar provision limiting the effect of 70a. There was, however, a considerable body of law compelled by considerations of justice and

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to the fact that such an amendment had the additional and more important consequence of eliminating protection for all transactions involving voluntary bankruptcies after the date of the filing of the petition.

equity that protected those who dealt in good faith with the bankrupt after bankruptcy. Section 70d was designed to eliminate the confusion that arose because of inconsistent judicial decisions. Its enactment was intended to set forth in an orderly fashion those good faith transfers where protection would be afforded. It was not, however, intended to codify all those transactions which were previously protected. (See: Analysis of H.R. 12889, 74 Cong. 2d Sess. (1936) 229-230; *McLaughlin,* 40 Harv. L. Rev. 583, 614; 4 *Collier on Bankruptcy,* Sec. 70.67, pages 1499, 1500.)

With the removal of section 70d from application to voluntary bankruptcies, the status of the law relating to bona fide transfers after bankruptcy is the same as it was prior to 1938. Notwithstanding the fact that the filing of the petition was said to be "caveat to all the world, and in effect an attachment and injunction," the courts prior to 1938, made exceptions to the doctrine where its application would work a hardship on an innocent party, who, following the inception of bankruptcy, dealt with the bankrupt on a bona fide basis for a present consideration. *Jones v. Springer,* 226 U.S. 148 (1912); *Frederick v. Fidelity Insurance Company,* 256 U.S. 395 (1921); *In re Locust Building Co. Inc.* (2nd Cir. 1924) 299 Fed. 756, certiorari denied sub. nom. *Keighley v. American Trust Co.,* 265 U.S. 590. It was recognized that where innocent parties were concerned, the mere filing of the petition gave rise to no notice that would put such persons on guard. *Frederick v. Fidelity Insurance Co.,* 256 U.S. 395 (1921); *In re Locust Building Co. Inc.* (2nd

Cir. 1924) 299 Fed. 756, certiorari denied sub. nom. *Keighley v. American Trust Co.,* 265 U.S. 590; *In re Raghman* (8th Cir. 1910) 183 Fed. 913; *Citizens National Bank v. Johnson* (6th Cir. 1923) 286 Fed. 527; *In re LaPlume Condensed Milk Company* (D.C.M.D. Penn. 1906) 145 Fed. 1013.

Cash sales were protected (*In re Peperall* (2nd Cir. 1921) 271 Fed. 466), as were payments by insurance companies in the ordinary course of business. (*Frederick v. Fidelity Insurance Company,* 256 U.S. 395 (1921).) Moreover, banks which honored checks of a depositor after bankruptcy, in good faith and without notice of the proceedings, were protected as against a subsequent claim to the money by the trustee. *In re Retail Stores Delivery Company* (D.C. S.D.N.Y. 1935) 11 F.Supp. 658; *Citizens National Bank v. Johnson* (6th Cir. 1923) 286 Fed. 527; *In re Fuller* (2nd Cir. 1923) 294 Fed. 71; *In re Zotti* (2nd Cir. 1911) 186 Fed. 84, certiorari denied sub. nom. *Watson v. European American Bank,* 223 U.S. 718; *Stevens v. Bank of Manhattan Trust Company* (D.C. S.D.N.Y. 1931) 11 F.Supp. 409; *In re Scranton Knitting Mills* (D.C.M.D. Penn. 1937) 21 F.Supp. 227; *In re Howe* (D.C. Mass. 1916) 235 Fed. 908, aff'd sub. nom. *Edison Electric Company v. Tibbets* (1st Cir. 1917) 241 Fed. 468.

Various reasons were adopted by the courts for not imposing liability against banks under such circumstances. It was said that the adage that "the filing of a petition is caveat to all the world," was not intended to apply to banks which honestly paid checks of a

depositor without notice of the bankruptcy. *In re Fuller* (2nd Cir. 1923) 294 Fed. 71; *In re Zotti* (2nd Cir. 1911) 186 Fed. 84, certiorari denied sub. nom. *Watson v. European American Bank,* 223 U.S. 718. The fact that the bank had an obligation to honor its depositors' checks was also held to support such a conclusion. *Stevens v. Bank of Manhattan Trust Company* (D.C.S.D.N.Y. 1931) 11 F.Supp. 409; *In re Howe* (D.C. Mass. 1916) 235 Fed. 908, aff'd sub. nom. *Edison Electric Company v. Tibbets* (1st Cir. 1917) 241 Fed. 468. Moreover, the fact that it was in the best interests of the free play of commerce was said to support a decision that a bank should not be held liable for honoring checks in good faith after bankruptcy. *In re Scranton Knitting Mills* (D.C.M.D. Penn. 1937) 21 F.Supp. 227.

However, the ground most frequently relied upon was the inequity of a contrary result. The courts recognized that it was virtually impossible for a bank to acquire notice of the bankruptcy of a depositor in order to protect itself against liability. The following statement from one of the earlier cases is typical.

> ". . . Its effect would be that the bank could not protect itself against liability to a trustee of bankruptcy subsequently appointed on account of payments made in good faith and in the regular course of business and in ignorance of the bankruptcy proceedings—except through the impossible course of keeping itself advised, not only daily, but momentarily, of the filing of petitions for adjudication of bankruptcy against depositors in any competent jurisdiction. In our opinion the bankruptcy works no such result. True, broadly

> speaking the adjudication when made relates back to the commencement of the bankruptcy proceedings for the purpose of adjudicating rights and equities generally (citing cases). But we think that both on principle and authority the rule referred to does not make the banker liable for good faith payments to third persons made before adjudication upon depositors' checks in the regular course of business and without the knowledge or notice of bankruptcy." *(Citizens National Bank v. Johnson* (6th Cir. 1923) 286 Fed. 527 at 528.)

The dilemma in which the bank is placed as expressed in the opinion set forth above is compounded by the fact that the bank owes an obligation to its depositors to honor their checks when they are presented for payment. (See: *New York County Nat. Bank v. Massey,* 192 U.S. 138 (1903); *Glassell Development Co. v. Citizens National Bank,* 191 Cal. 375, 216 Pac. 1012 (1923); *Weaver v. Bank of America,* 59 C.2d 428, 380 P.2d 644 (1963).) This was recognized by the Ninth Circuit in this very case:

> "The bank's dilemma is real since it is under a duty to depositors to honor checks which are validly drawn; at the same time there is always a possibility that the depositor, without the knowledge of the bank, has become the subject of bankruptcy proceedings. The hardship to the bank in keeping itself apprised of developments in the bankruptcy court is contrasted with the relatively light burden that a notice requirement would place upon the trustee. The trustee or receiver, upon filing, is informed of the bankrupt's accounts and deposits; and notification by him to the bank would be relatively simple." (R111.)

The fact that many of the cases discussed above dealt with situations where the transaction occurred prior to adjudication is not a distinguishing factor. Although the enactment of section 18f in 1959 made adjudication automatic upon the filing of a voluntary petition, the doctrine of "relation back", which has been consistently applied by the courts in the past, effected the same result by holding that the trustee's title vested as of the date of the petition. See: *Everett v. Judson,* 228 U.S. 474 (1913); *Andrews v. Partridge,* 228 U.S. 479 (1913); *Acme Harvester v. Beekman Lumber Company,* 222 U.S. 300 (1911); *Zavelo v. Reeves,* 227 U.S. 625 (1913); *Fairbanks Steam Shovel Company v. Wills,* 240 U.S. 642 (1916).

More importantly, the constitutional objections that have previously been discussed apply with equal force to the lack of notice that accompanies adjudication as to the insufficiency of notice attendant to the filing of a voluntary petition. Adjudication does not make the filing any more notorious. That fact was recognized in *Frederick v. Fidelity Mutual Insurance Company,* 256 U.S. 395, 398-399 (1921). The *Frederick* case is particularly significant since it held that a transfer made after adjudication was valid where no notice of the filing of the petition or of adjudication had been given. In *Frederick,* the bankrupt owned a life insurance policy which had a cash surrender value at the time the petition was filed. The bankrupt died and the insurance company paid the full value of the policy to the beneficiary. The company at no time prior to payment had notice of the filing of the petition or of the adjudication. The trustee then filed suit to recover

the surrender value of the policy as of the date of adjudication, basing his claim on Bankruptcy Act section 70a. The Court, in holding that the company was not liable to the trustee unless it had been given notice, stated (at page 398):

> "It is not enough to sustain the trustee's claim to say that the filing of the petition in bankruptcy was a caveat to all the world, and in effect an attachment and injunction, and that, on adjudication, title to the bankrupt's properties became vested in the trustee. . . ."

With the practical elimination of section 70d from application to voluntary proceedings, there are no limitations set forth in the Act defining the limits of protection which conflict with the results of the earlier decisions. The numerous reasons that have constrained courts of bankruptcy in the past to exercise their equitable powers to protect good faith payments by a bank after bankruptcy are present here.

C. Well established equitable principles provide that the bank be protected in its payment.

Courts of bankruptcy are essentially courts of equity and may exercise broad equitable powers to protect hardship and unfairness. *Local Loan Company v. Hunt,* 292 U.S. 234 (1934); *Pepper v. Litton,* 308 U.S. 295 (1939); *Securities and Exchange Commission v. United States Realty and Improvement Company,* 310 U.S. 434 (1934); Bankruptcy Act section 2, 52 Stat. 842 (1938), 11 U.S.C. 11(a). The unfairness of the Court of Appeals' ruling is obvious. The Bank of Marin, which was under a legal obligation to honor

the checks of its depositor, Marin Seafoods, honored the checks in good faith. By so doing, the bank has been held liable to the trustee for a sum equivalent to that paid even though the bank had no knowledge of the bankruptcy. The only means by which the bank could have protected itself from being placed in this dilemma was to ascertain whether or not the depositor had filed a voluntary petition of bankruptcy in any District Court in the United States before it honored the checks. The very magnitude of such a task renders it impossible.

Opposed to the virtually impossible duty that is placed upon the bank, the trustee could easily have notified the bank by mail or by telephone of the fact that a voluntary petition had been filed. The bank account was listed in the schedules filed by the bankrupt and the name and address of the bank were readily available.

The inequity of the holding of the Court of Appeals is emphasized by the potential exposure to liability that is placed upon banks. Although this case involves only a few checks amounting to several thousand dollars, a similar situation involving many times that amount of money is not remote. In contrast to the virtually unlimited exposure placed upon banks, is the fact that the bankruptcy estate would be losing nothing if banks were protected. Any payment to a third party by the bankrupt which occurs so close to the moment of bankruptcy that the check is presented for payment after the filing of a voluntary petition would be a preference (Bankruptcy Act section 60, 64

Stat. 24 (1950), as amended, 11 U.S.C. 96) or a fraudulent transfer (Bankruptcy Act section 67, 66 Stat. 427 (1952), 11 U.S.C. 107) and recoverable by the trustee from the payee.

III

THE NEGOTIABILITY PROVISION OF SECTION 70d(5) OF THE BANKRUPTCY ACT PROTECTS A BANK WHICH HONORS CHECKS OF A BANKRUPT DEPOSITOR IN GOOD FAITH WITHOUT NOTICE OF THE BANKRUPTCY.

In holding that the bank is liable to the trustee for an amount equivalent to the sums it paid in honoring the checks of its bankrupt depositor, the Court of Appeals stated that the "negotiability" provision of Bankruptcy Act section 70d(5) does not apply. The Court put forward two reasons as justifying such a conclusion.

First, it stated that the introductory words to section 70d indicate that it applies only to transactions taking place during the interval between the filing of the petition and adjudication or the taking of possession by a receiver. Since in the case of a voluntary petition, there is no such interval, section 70d(5) was said to have no application.

The Court of Appeals ignored the plain meaning of the last sentence of section 70d(5) which reads, "Provided, however, that nothing in this title shall impair the negotiability of currency or negotiable instruments." That provision appears on its face to apply to all of Title 11 of the United States Code (the

Bankruptcy Act). It is not dependent upon any other provision of the Bankruptcy Act or the remainder of section 70d for its application. The fact that the other portions of section 70d do not apply to voluntary bankruptcies has no bearing on the effect of the negotiability proviso.

Secondly, the Court of Appeals stated that the negotiability clause did not afford protection to the bank since presentment of a check to the drawee bank for payment, and payment thereof, is not a technical negotiation. However, the negotiability proviso of section 70d(5) does not limit its application to parties to a negotiation or, for that matter, to a holder in due course. Protection is afforded to anyone whose relationship to a transaction involving a negotiable instrument is such that the negotiability of that instrument would be impaired if liability were imposed upon such person.

Negotiability gives the holder of a negotiable instrument maximum assurance that he will be able to collect on such document without any defenses being interposed. It is that characteristic which permits such documents to flow freely in the commercial world and to be utilized as a substitute for money. It is difficult to imagine a situation where the concept of negotiability is more seriously hampered by bankruptcy than by holding a drawee bank responsible for honoring checks of a bankrupt depositor in good faith without notice of the bankruptcy. The entire risk of loss in untold instances would be placed upon a bank which is the only party to such a transaction acting

in good faith, as a mere conduit for payment. On the other hand, the bankrupt is obviously aware of the ramifications of his act and the payee will generally be a preferred creditor (Bankruptcy Act section 60) or a fraudulent transferee (Bankruptcy Act section 67).

Moreover, the only means by which the bank could avoid the consequences of the Court of Appeals' decision would be to delay acceptance of a check until such time as it could be ascertained that the bank's depositor was not in bankruptcy. This would not only violate the bank's legal obligation to its depositor to honor the check upon presentment, but would also destroy the freedom with which checks flow in the commercial world and their usefulness as a substitute for money.

It is inconceivable that Congress, in enacting section 70d(5), intended to eliminate from its protective coverage the party that most frequently would be involved in the negotiation of checks, that is, the drawee bank. This is particularly true since the negotiability provision would afford little protection to the payee. Is it not more probable that Congress intended this exception primarily for the protection of banks upon whom the orderly flow of the country's money depends and to whom it is entrusted under Federal and State regulations?

The one other reported decision that has dealt with the issue presented in this petition adopted the reasoning set forth above and held that the negotiability provision of section 70d(5) protected a bank which

honored checks in good faith after the adjudication of bankruptcy of its depositor without notice. *Rosenthal v. Guaranty Bank & Trust Co.* (D.C. La. 1956) 139 F.Supp. 730.[4]

The reasoning of the *Rosenthal* decision is best set forth in the following quotation:

> "The Trustee particularly directs the Court's attention to Subparagraph (5) of Title 11 U.S.C.A. Section 110, subdivision d, which he says plainly and expressly states that except as provided in subdivision d and in subdivision g of Section 44 (which latter subdivision relates to real estate and has no bearing here), no other transfer after the date of the bankruptcy shall be valid against the Trustee, and of course, he argues, the only exceptions stated in subdivision d are that the payments must be made both before adjudication and without notice of the pending proceedings.
>
> "This argument is not without merit and were it not for the fact that there is appended to that Section the proviso 'that nothing in this title shall impair the negotiability of currency or negotiable instruments', we would be inclined to agree. Since no court decision has been called to our

[4]Although the *Rosenthal* case arose under a voluntary petition for corporate reorganization pursuant to Chapter X of the Bankruptcy Act, Chapters I through VII apply (Bankruptcy Act section 102, 11 U.S.C. 502). The Court concluded that the date of adjudication was the date of the approval of the petition for reorganization.

The petition was filed on October 3, in the District Court of New York and was approved that same day. Subsequently, from October 4 to October 10, the defendant, a Louisiana bank, honored checks totaling approximately $7,000 without actual knowledge of the bankruptcy.

attention and none have been found interpreting the meaning or purpose of this provision, the matter must be considered res integra. When the bankruptcy occurs the bank upon which the bankrupt drew a check prior to the date of the bankruptcy finds himself caught in the intermeshing of two highly complicated systems of law. Traditionally, it is the primary function of the Bankruptcy Act to protect the creditors, to marshal the assets, and to distribute them among the creditors equitably and ratably in accordance with their respective rights and interests. Negotiability tries to give the bank the maximum assurance that it will be able to cash the check without any defenses being interposed. An expansion of bankruptcy in some senses indisputably hinders the flow of commercial paper. *In the absence of any prior interpretation, we agree with counsel for defendants that one of the purposes of the 'negotiability' provision in the Bankruptcy Act was to protect a bank in a case of this kind, if the bank was in good faith and had no 'actual knowledge' of the pending bankruptcy." (Rosenthal v. Guaranty Bank and Trust Company* (D.C. La. 1956) 139 F.Supp. 730 at 734; emphasis added.)

The Court in *Rosenthal,* in addition to determining that the negotiability proviso of section 70d(5) was intended to protect drawee banks, held that it applied to transfers occurring after adjudication.[5] No reason

[5]The checks that were honored by the bank in *Rosenthal v. Guaranty Bank and Trust Company* (D.C. La. 1956) 139 F.Supp. 730 were honored after adjudication.

Although the technical adjudication of bankruptcy for the purposes of corporate reorganization did not occur for almost

exists for distinguishing between transfers occurring before or after adjudication insofar as section 70d(5) is concerned. The very language of the negotiability proviso of section 70d(5) indicates that it is not to be restricted by any other provision in the Act. The proviso does not appear in the introductory language of section 70d(5), but as a qualification to section 70d(5), which deals with all transfers occurring after bankruptcy. Since transfers occurring either prior or subsequent to adjudication fall into this category, the negotiability proviso applies in either situation.

The negotiability proviso of section 70d(5) protects the Bank of Marin in honoring the checks of its depositor, Marin Seafoods, under the facts of this case. Any other interpretation of that section would distort the plain meaning of the terms used and the obvious intent of Congress in enacting such a provision.

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three years after the filing of the petition, the Court in *Rosenthal* considered the date of the filing of the petition as the date of adjudication for the purpose of interpreting Bankruptcy Act section 70a and for determining the issue presented.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that the judgment of the Court of Appeals for the Ninth Circuit be reversed and the cause remanded to the District Court for entry of the appropriate order in favor of the Bank of Marin.

Dated, San Rafael, California,
July 20, 1966.

CARLOS R. FREITAS,
BRYAN R. MCCARTHY,
EDGAR B. WASHBURN,
FREITAS, ALLEN, MCCARTHY & BETTINI,
Counsel for Petitioner.

(Appendix Follows)

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Appendix

United States Constitution Amendment V:

> No person shall be . . . deprived of life, liberty or property without due process of law.

Bankruptcy Act section 18(f), 73 Stat. 109 (1959), 11 U.S.C. 41(f):

> The filing of a voluntary petition under chapters 1 to 7 of this title, other than a petition filed in behalf of a partnership by less than all of the partners, shall operate as an adjudication with the same force and effect as a decree of adjudication.

Bankruptcy Act section 70, 52 Stat. 879-881 (1938) as amended, 11 U.S.C. 110: Title to property:

> (a) The trustee of the estate of a bankrupt and his successors, if any, upon his or their appointment and qualification, shall in turn be vested by operation of law with the title of the bankrupt as of the date of the filing of the petition initiating a proceeding under this title, except insofar as it is to property which is held to be exempt, to all of the following kinds of property wherever located . . . property, including rights of action, which prior to the filing of the petition he could by any means have transferred or which might have been levied upon and sold under judicial process against him or otherwise seized, impounded, or sequestered. . . .
>
> . . .
>
> (d) After bankruptcy and either before adjudication or before a receiver takes possession of the property of the bankrupt, whichever first occurs—
>
> . . .

(1) A transfer of any of the property of the bankrupt, other than real estate, made to a person acting in good faith shall be valid against the trustee if made for a present fair equivalent value or, if not made for a present fair equivalent value, then to the extent of the present consideration actually paid therefor, for which amount the transferee shall have a lien upon the property so transferred;

(2) A person indebted to the bankrupt or holding property of the bankrupt may, if acting in good faith, pay such indebtedness or deliver such property, or any part thereof, to the bankrupt or upon his order, with the same effect as if the bankruptcy were not pending;

(3) A person having actual knowledge of such pending bankruptcy shall be deemed not to act in good faith unless he has reasonable cause to believe that the petition in bankruptcy is not well founded;

(4) The provisions of paragraphs (1) and (2) of this subdivision shall not apply where a receiver or trustee appointed by a United States or State court is in possession of all or the greater portion of the non-exempt property of the bankrupt;

(5) A person asserting the validity of a transfer under this subdivision shall have the burden of proof. Except as otherwise provided in this subdivision and in subdivision g of section 44 of this title, no transfer by or in behalf of the bankrupt after the date of bankruptcy shall be valid against the trustee: Provided, however, That nothing in this title shall impair the negotiability of currency or negotiable instruments.

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AMICUS CURIAE BRIEF

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In the Supreme Court of the United States

OCTOBER TERM, 1965

No. [redacted] 63

BANK OF MARIN,
Petitioner,

vs.

JOHN M. ENGLAND, Trustee in Bankruptcy,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

Brief of California Bankers Association, Amicus Curiae, in Support of Petitioner

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Brief of California Bankers Association, Amicus Curiae, in Support of Petitioner

By consent of petitioner, Bank of Marin, and of respondent, John M. England, Trustee in Bankruptcy, filed herewith, the California Bankers Association files this brief as amicus curiae in support of petitioner.

STATEMENT OF INTEREST OF THE AMICUS CURIAE

The amicus curiae, the California Bankers Association, is a nonprofit California corporation, the membership of which is composed of commercial banks operating in the State of California. It is interested in this litigation for

the following reasons: The United States Court of Appeals for the Ninth Circuit has held that a bank which honors checks of one of its depositors after that depositor has filed a voluntary petition in bankruptcy is liable to the Trustee in Bankruptcy for the amount of those checks, although the bank made payment in good faith and without notice of the bankruptcy proceeding. Since banks are under a legal obligation to honor checks of their depositors duly presented, and since it is impossible for banks to keep themselves currently advised of all petitions in bankruptcy affecting their depositors, affirmance of that ruling would result in great and unprotectable loss to the banking industry in California.* Accordingly, this litigation is of vital interest to the banks of this State.

SUMMARY OF ARGUMENT

The amicus curiae agrees with and supports each argument advanced by the petitioner in its opening brief. In order to supplement petitioner's argument and to avoid repetition, the amicus curiae will restrict its brief to the following two arguments:

First: Upon the filing of a petition in bankruptcy, the Trustee in Bankruptcy succeeds only to such rights as are possessed by the bankrupt. In this case, the bankrupt would have been entitled to recover the amount of the checks which petitioner honored pursuant to its order only if it had revoked that order prior to the time of payment. Since no such "stop payment" order (or notice of the bankruptcy proceeding) was given, the trustee, as the bankrupt's successor, is also barred from recovery.

Second: Even if payment of those checks constituted a transfer rendered invalid by Section 70(d)(5) of the

*For discussion of the extent of that loss, see p. 9, *infra*.

Bankruptcy Act (11 U.S.C. § 110(d)(5)), that provision does not require this Court to hold *both* petitioner and the payee of the checks liable to the trustee. In equity and in fairness, it should not do so.

ARGUMENT

A. The Failure of the Trustee to Revoke the Bankrupt's Order for the Payment of Funds on Deposit with the Petitioner or to Give Notice of the Bankruptcy Proceeding Bars the Trustee from Recovery Against the Petitioner

In granting recovery to the Trustee, the courts below relied on Section 70(a) of the Bankruptcy Act, (11 U.S.C. § 110(a)). This section provides in part:

> "The trustee of the estate of a bankrupt and his successor or successors, if any, upon his or their appointment and qualification, shall in turn be vested by operation of law with the title of the bankrupt as of the date of the filing of the petition initiating a proceeding under this title, . . . to . . . (5) property, including rights of action, which prior to the filing of the petition he could by any means have transferred. . . ."

Under that provision a trustee in bankruptcy succeeds *only* to such rights as the bankrupt possessed at the time of the filing of the bankruptcy petition, and is subject to all claims, defenses and equities which might have been asserted against the bankrupt but for the filing of that petition.

Zartman v. First Nat'l Bank, 216 U.S. 134, 138 (1910);

In re Woodruff, 272 F.2d 696, 699 (7th Cir. 1959);

Schultz v. England, 106 F.2d 764, 768 (9th Cir. 1939);

4 Collier, *Bankruptcy*, p. 1244 (14th ed.).

Thus, for example, where a trustee asserts a claim based upon a contract between the bankrupt and a third party, the trustee's rights against that third party depend upon the terms of the contract and are no greater than those which the bankrupt might have exercised thereunder.

See,

Christensen v. Felton, 322 F.2d 323 (9th Cir. 1963);
Hummel v. Equitable Life Assur. Soc., 151 F.2d 994 (7th Cir. 1945);
Schultz v. England, supra.

Accordingly, in determining whether the trustee in this case is entitled to recover from petitioner, it is first necessary to ascertain the nature and extent of the rights of the bankrupt against the petitioner.

It is well established both in California and elsewhere that an ordinary depositor does not have title to any specific funds which he deposits in a bank: the relationship of bank and depositor is that of debtor and creditor, and is founded upon contract.

See,

Anderson Nat'l Bank v. Luckett, 321 U.S. 233, 248 (1944);
Dix v. Bank of California Nat'l Ass'n., 113 F. Supp. 823, 825 (N.D. Cal. 1952), *aff'd sub nom. Dix v. Pineda,* 205 F.2d 957 (9th Cir. 1953);
Basch v. Bank of America Nat'l Trust & Sav. Ass'n., 22 C.2d 316, 321, 139, P.2d 1 (1943).

Under that contract, a bank has the right and the duty to honor checks of its depositor properly drawn and duly presented.

See,

Anderson Nat'l Bank v. Luckett, supra;
Basch v. Bank of America Nat'l Trust & Sav. Ass'n., supra;
Brady, *Bank Checks,* § 12.3 (3d ed.).

The depositor may revoke his order for payment from his account by giving the bank notice thereof prior to the time his checks are accepted or paid by the bank.

See,

California Financial Code § 990;*
Brady, *op. cit. supra,* §§ 10.7, 13.1, 13.3.

But absent revocation by a timely "stop payment" notice, payment by the bank operates to discharge its obligation under that contract, and the depositor has no right to recover the amounts paid.

See,

Basch v. Bank of America Nat'l Trust & Sav. Ass'n., supra;
Brady, *op. cit. supra,* §§ 10.7, 10.8, 13.1, 13.3.

The applicability of those basic principles to the facts of this case is self apparent. Prior to the filing of its voluntary petition in bankruptcy, Marin Seafoods, Inc., drew checks totaling the sum of $2,312.82 upon the petitioner, with which it had a commercial account (R. 45-46); the checks were drawn in favor of a creditor of the bankrupt, Eureka Seafoods, and were outstanding on September 26, 1963, the date of the filing of that petition (R. 46). Those checks were honored by the petitioner on October 2, 1963 (R. 46).

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*This statute was repealed as of January 1, 1965, with the adoption of the Uniform Commercial Code in California. Section 4403 of the Uniform Commercial Code embodies the same principle.

At no time on or before that date did the bankrupt or the Trustee in Bankruptcy revoke the bankrupt's order for payment of those checks or inform the petitioner of the bankruptcy proceeding. (R. 47.) Under these circumstances, the bankrupt would have had no right to recover the amount of those checks from the petitioner. Accordingly, the Trustee is also barred from recovery, and the lower court's judgment should be reversed accordingly.

The Court of Appeals below rejected the foregoing contention on the ground that:

> "The bankruptcy of a drawer operates as a revocation of the drawee's authority. Such revocation is not dependent upon or subject to notice of the drawee, since the trustee is immediately vested with the title of the bankrupt by operation of law. . . . These circumstances constitute an implied exception to the contractual obligation of the bank to honor checks unless and until a 'stop payment' notice is received." (352 F.2d at 191 (R. 113).)

In support of its conclusion that the bankruptcy of a drawer operates as a revocation of the drawee's authority, the court cited the following authorities: *Harrison State Bank v. First Nat'l Bank,* 116 Neb. 456, 218 N.W. 92 (1928); *Guthrie Nat'l Bank v. Gill,* 6 Okla. 560, 54 Pac. 434 (1898); and Brady, *Bank Checks,* p. 25 (3d ed.). The amicus curiae submits that none of those authorities support that conclusion: all are consistent with the general principles set forth above.

Harrison State Bank v. First Nat'l Bank, supra, involved an action against a drawee bank which had refused to honor drafts by one of its depositors, a second bank, *after it had received notice* that the depositor was insolvent and had been ordered closed by the Comptroller of the Cur-

rency. The Nebraska Supreme Court merely held the defendant not liable to the payee of those drafts for having refused payment after receipt of such notice.

In *Guthrie Nat'l Bank v. Gill, supra,* defendant bank had refused to honor a check *where it had notice* that after the check was drawn the drawer had made an assignment for the benefit of the creditors. Here, again, the court simply ruled that the defendant was not liable to the payee for having refused payment.

Brady, *Bank Checks,* p. 25 (3d ed.), merely cites the same two inapposite cases as authority for the statement that:

> "In the absence of statute, bankruptcy or insolvency of a drawer of checks operates as a revocation of authority of the drawee bank to pay uncertified checks outstanding."

However, Brady continues as follows:

> "A bank has been held liable in paying a check issued after the drawer made an assignment for the benefit of creditors, where the bank *had knowledge* of drawer's insolvency, even though the check was dated prior to the assignment. *But a bank paying a check in good faith in ignorance of drawer's bankruptcy or insolvency is protected in its payment.*" (Emphasis added.)

For the latter proposition, Brady cites two cases, *Citizens Union Nat'l Bank v. Johnson,* 286 Fed. 527 (6th Cir. 1923) and *Rosenthal v. Guaranty Bank & Trust Co.,* 139 F. Supp. 730 (D.C. La. 1956). Both of those cases, considered in the brief of the petitioner, lend additional support to the view that a bank fulfilling its contractual obligation to its depositor without notice of his bankruptcy is entitled to protection under the law.

See also,

In re Howe, 235 Fed. 908 (D. Mass. 1916), *affirmed sub nom. Edison Elec. Illuminating Co. v. Tibbetts*, 241 Fed. 468 (5th Cir. 1917).

B. Even Assuming That Payment of the Checks in Question Constituted an Invalid Transfer as Against the Respondent, Recovery Should Not Be Permitted Against the Petitioner

The Court of Appeals below also based its decision upon the ground that payment of the bankrupt's checks after the filing of its voluntary petition constituted a transfer which is invalid against the respondent under Section 70(d)(5) of the Bankruptcy Act (11 U.S.C. § 110(d)(5)). That section provides in part as follows:

> "Except as otherwise provided in this subdivision and in subdivision g of Section 44 of this title, no transfer by or in behalf of the bankrupt after the date of bankruptcy shall be valid against the trustee . . ."

The amicus curiae believes that this contention has been adequately answered by the brief of the petitioner and in the preceding section of this brief. For the purposes of argument, however, the amicus curiae will assume that the payment of those checks did constitute such a transfer. Even on that assumption, petitioner should not be held jointly liable with the payee of those checks.

Prior to the enactment of Section 70(d), there was considerable confusion in the cases as to which of those transactions occuring between the filing of a petition in bankruptcy and adjudication were to be protected against the claims of the trustee. Section 70(d) was enacted to end that confusion by specifically designating certain transactions entitled to protection.

See,

H.R. Rpt. No. 1409, 75th Cong., 1st Sess. 35 (1937); National Bankruptcy Conference, Analysis of H.R. 12889, 74th Cong., 2d Sess., 229-31 (1936); 4 Collier, *op. cit, supra,* para. 70.66, 70.67.

But there is nothing in the language or the legislative history of that provision which compels this Court to rule that the trustee is entitled to judgment against both the transferee-payee of those checks and the transferor-bank. For the reasons set forth below, it is submitted that the Court should not do so in this case.

That there is no equitable basis for permitting recovery against the petitioner can scarcely be disputed. Petitioner paid out the amounts in question in good faith, and in reliance upon its contractual obligation to honor checks of its depositor. At the time it did so, petitioner had no notice whatever of the bankruptcy proceeding (R. 47), although the respondent was aware of the bankrupt's account with the petitioner and could very easily have provided such notice (R. 2, 9, 46). Since it is obviously impossible for banks to keep themselves informed hour by hour of the filing of all voluntary petitions in every district court in every state which may affect their depositors, affirmance of the lower court's judgment would render banks subject to repeated and substantial judgments against which they have no effective means of protection.*

The justification for imposing liability on the payee of those checks is readily apparent. Eureka Fisheries is an

*The Court of Appeals below recognized the bank's "dilemma" and the "hardship and impracticability" of "timely discovery of bankruptcy proceedings involving [a bank's] depositors." (352 F.2d at 190 (R. 111.)) But it went on to suggest that since *Rosenthal v. Guaranty Bank & Trust Co.*, 139 F. Supp. 730 (D.C. La. 1956), is the only previously reported case dealing with the question presented herein, that question is not one which will

unsecured trade creditor of the bankrupt, to which the bankrupt was indebted for merchandise delivered (R. 12). In its dealings with the bankrupt it voluntarily assumed the risks incident to a credit relationship, including the risk of bankruptcy. Yet, by reason of the transfers involved herein, that creditor received payment of its claims after its debtor had filed a petition in bankruptcy. Requiring that creditor to pay the trustee the amount of the funds

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frequently confront banks and, therefore, does not threaten banks with great financial loss. That inference is mistaken.

Prior to the enactment of the present Section 18(f) (11 U.S.C. 41(f)) of the Bankruptcy Act in 1959, there was an interval between the date of the filing of both a voluntary and an involuntary petition and the adjudication of bankruptcy. At the time of that enactment it was well settled that a bank honoring checks of its depositor during that interval without notice of a bankruptcy proceeding affecting that depositor was entitled to protection against the claims of a trustee. See, Bankruptcy Act, § 70(d) (11 U.S.C. 110 (d)); *Citizens National Bank v. Johnson,* 286 Fed. 527 (6th Cir. 1923); *In re American Foam Rubber Corp.,* 222 F. Supp. 679 (S.D. N.Y. 1963). That interval provided banks with an opportunity to become advised of the pendency of the bankruptcy proceeding prior to adjudication and to protect themselves accordingly. For that reason, the question presented herein did not arise.

As enacted in 1959, Section 18(f) of the Bankruptcy Act eliminated that interval in the case of voluntary petitions by making the time of adjudication coincidental with the filing of the petition in bankruptcy. Nonetheless, it was generally assumed by banks and trustees in bankruptcy alike that that enactment was not intended to and did not operate to deprive banks of the protection which has theretofore been afforded. *Rosenthal v. Guaranty Bank & Trust Co., supra,* lent support to that assumption.

Since the decision of the District Court below in 1964, however, trustees have with increasing frequency asserted claims similar to those asserted by the respondent herein. The amicus curiae has been advised by one of its members, Bank of America National Trust & Savings Association, that since that time such claims have been asserted against it in six voluntary bankruptcy proceedings. Other banks operating in this State have reported similar experiences since the date of that decision. Given these considerations, and the large and increasing number of voluntary petitions in bankruptcy filed in this State, and throughout the country, every day, affirmance of the lower court's judgments would inevitably result in a very substantial loss to the banking industry.

so received would place it in no worse a position than before those transfers: It would merely be deprived of what amounts to a preferential payment of its claims and restored to its proper position as a general creditor of the bankrupt.

Imposition of liability upon the petitioner would have very different consequences. The petitioner was not a creditor of the bankrupt prior to its bankruptcy, and did not undertake the risks of a creditor in dealing with the bankrupt. The petitioner has received no benefit whatever from the transactions involved herein, but has merely paid out funds in satisfaction of its contractual obligation to one of its depositors. Accordingly, a judgment against petitioner would not deprive it of a benefit obtained at the expense of other creditors of the bankrupt, nor restore it to its prior position vis a vis the bankrupt.* Rather, as noted in the brief of the petitioner, such a judgment would result in the petitioner's having to pay the same debt twice.†

If this were a case in which the Court had to decide which of two innocent parties, the bank or the general creditors of the bankrupt, must ultimately bear the consequences of the bankrupt's action, it may be that the loss should fall upon the bank. But this is not such a case. Similarly, if the trustee had notified the petitioner of the bankruptcy pro-

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*Petitioner would not even have a provable claim against the bankrupt's estate, since it arose after adjudication. See Bankruptcy § Act 63(a) (11 U.S.C. § 103(a)). And any claim of the petitioner against its bankrupt corporate depositor apart from bankruptcy would be worthless.

†Eureka Fisheries has satisfied the joint judgment rendered by the District Court below against it and the petitioner, but it has also filed a claim for contribution against the petitioner in the bankruptcy court (R. 54-55). Regardless of the merits of that claim this Court, in the exercise of its equitable powers, should reverse the lower court's judgment to avoid unnecessary circuity and multiplicity of action.

ceeding promptly, as it could easily have done, imposition of liability upon the petitioner might be justified. But the trustee failed to do so. It is therefore submitted that the Court should protect both the petitioner and those general creditors, and permit the trustee to obtain recovery only against that party which benefited from the subject transactions.

Support for the position of the amicus curiae is found in *In re Howe,* 235 Fed. 908 (D. Mass. 1916), *affirmed sub nom. Edison Elec. Illuminating Co. v. Tibbetts,* 241 Fed. 468 (1st Cir. 1917), a case involving facts closely parallel to that involved herein. There, both courts recognized that the payment of checks of a bankrupt following an adjudication of bankruptcy constituted an invalid transfer as against the trustee, and held the trustee entitled to recover the value of those checks from the payee. But the courts also recognized that despite the invalidity of that transfer, the trustee might be denied recovery in a suit against the drawee bank.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that the judgment of the Court of Appeals for the Ninth Circuit should be reversed.

Dated: August 19, 1966.

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Supreme Court of the United States

OCTOBER TERM, 1966

No. 63

BANK OF MARIN, *Petitioner*

vs.

JOHN M. ENGLAND, Trustee in Bankruptcy, *Respondent.*

On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

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Brief for Respondent

STATEMENT OF THE CASE

Respondent agrees with Petitioner that the facts are not in dispute. Two matters, however, require brief comment.

First, Petitioner has expressed in its Statement of the Case the following erroneous conclusion of law: Petitioner asserts that since the referee held the Bank of Marin and Eureka Fisheries jointly liable to the trustee for the sum of $2,312.82, and since Eureka Fisheries paid said sum to the trustee and served upon the bank a notice of payment and demand for contribution pursuant to California Code of Civil Procedure Section 709, Eureka Fisheries thereby

became entitled "to the remedy of execution to recover from the bank one-half the amount Eureka Fisheries paid on the joint judgment." (Petitioner's Brief, p. 4.) Petitioner implies that the remedy of execution is immediately available to Eureka Fisheries "without the necessity of further proceedings." (Petitioner's Brief, p. 5, footnote 1.) Respondent's view that the law is to the contrary is fully set forth below at pp. 22-23.

Secondly, Respondent is obliged to inform the Court that his pecuniary interest in the final disposition of this case is limited. The judgment of the referee held Petitioner severally liable to Respondent for $700.47, and jointly liable with Eureka Fisheries to Respondent for the further sum of $2,312.82. (R. 48.) Eureka Fisheries did not appeal, and Petitioner did not appeal from the several judgment against it in the sum of $700.47. (R. 50-51.) The only part of the judgment which has not become final, therefore, is the joint judgment for $2,312.82 in favor of Respondent against Petitioner. (R. 50-51.) Meanwhile, Eureka Fisheries has satisfied the joint judgment by payment in full to Respondent. (R. 54-55.) In this posture, Respondent believes he cannot be deprived of any recovery heretofore received and, thus, that Respondent's sole financial interest herein is to protect against the imposition of costs pursuant to the provisions of Rule 57 of the Rules of this Court.

The foregoing is not intended as a retreat from Respondent's legal position that a bank is liable to a trustee in bankruptcy for cashing checks of a bankrupt depositor subsequent to the filing of such depositor's voluntary petition in bankruptcy despite the bank's lack of actual knowledge of the filing of such voluntary petition. Respondent urges that the decision of the Court of Appeals was correct and should be sustained.

SUMMARY OF ARGUMENT

Prior to 1938, the Bankruptcy Act did not clearly define the right of persons dealing, after bankruptcy, with assets of bankrupt estates. Relief was provided, however, under the judicial doctrine of "protected transactions," to persons acting in good faith although the doctrine was imprecise and led to constant litigation.

To resolve the confusion, Congress, in 1938, codified the "protected transaction" doctrine in Section 70d of the Bankruptcy Act. By its terms Section 70d establishes an unequivocal dividing line between protected and unprotected transactions. The conduct of the bank in this case, in honoring, after adjudication, checks drawn on an account that was an asset of a bankrupt estate falls outside the scope of the transactions afforded protection.

Notwithstanding the foregoing, Petitioner claims that it is entitled to protection because the transaction involved the payment of checks. Petitioner relies upon the provision of Section 70d(5) that "nothing in this Act shall impair the negotiability of negotiable instruments," but the negotiability proviso does not apply in this case involving the presentment of checks to a drawee bank for collection.

Petitioner also claims that because the trustee may recover from third parties he should be precluded from asserting his claim against Petitioner. No basis exists for such a restrictive application of Sections 70a and 70d. If Petitioner's view were adopted, the power of the trustee to collect assets of bankrupt estates would be impaired.

The history of the "protected transaction" doctrine and its codification as Section 70d dispels any doubt that Congress acted deliberately and with full consideration of Petitioner's dilemma. This history shows that a real need existed for the adoption of Section 70d and that consider-

able thought was given to the dividing line between protected and unprotected transactions. The rule adopted is a legitimate exercise of legislative discretion, and if the rule is too harsh, Petitioner should direct its criticism to Congress.

The foregoing is especially true in a case such as that now before this Court. Petitioner has paid nothing on the joint judgment. We doubt that Petitioner ever will have to pay as a result of the joint judgment now being reviewed. Even if Petitioner is later required by state court proceedings to contribute to the third party who previously satisfied the joint judgment herein, there is no basis for Petitioner's claim that it would thereby be required to pay the same debt twice. Petitioner made one payment voluntarily under mistake of fact. Petitioner cannot assert its mistaken payment to a third party as a defense to the trustee's claim.

ARGUMENT

I. A Bank Is Accountable to a Trustee in Bankruptcy When It Honors a Depositor's Checks Against Assets of the Bankrupt Estate After the Depositor Has Been Adjudicated a Bankrupt.

The fundamental issue herein is whether Petitioner, the Bank of Marin (sometimes hereinafter referred to as "the bank"), may properly be held liable to Respondent, a trustee in bankruptcy (sometimes hereinafter referred to as "trustee"), for disbursing the bankrupt's post-adjudication deposits resulting from the collection by the bankrupt of pre-adjudication receivables.

The governing statutory rule is that

> "The trustee of the estate of a bankrupt . . . upon his . . . appointment and qualification, shall . . . be vested by operation of law with the title of the bankrupt as of the date of the filing of the petition initiating a proceeding under this Act . . . to all . . . (5) property,

> including rights of action, which prior to the filing of the petition he could by any means have transferred . . . ." Bankruptcy Act § 70a, 52 Stat. 879 (1938), as amended, 11 U.S.C. § 110(a).

Section 70d of the Bankruptcy Act (52 Stat. 881 (1938), 11 U.S.C. § 110(d)) further provides (in pertinent part) that "no transfer by or in behalf of the bankrupt after the date of bankruptcy shall be valid against the trustee."

The Collier treatise interprets Section 70a as follows:

> "The title of the bankrupt vests in the trustee, 'as of the date he was adjudicated a bankrupt,' but upon thus vesting relates back to the time of the filing of the petition. While it is true that by subsection *a* the trustee, upon his appointment and qualification, becomes vested by operation of law with the title of the bankrupt as of the date he was adjudged a bankrupt, there are other provisions of the statute which evidence the intention to vest in the trustee the title to such property as it was at the time of the filing of the petition, the estate being considered as *in custodia legis* from that time." 4 COLLIER, BANKRUPTCY Sec. 70.05, p. 963 (14th Ed. 1964).

Petitioner does not assert that Respondent failed in the performance of any duty imposed upon him by the Bankruptcy Act or otherwise to notify Petitioner simultaneously of the fact of the bankrupt's adjudication. No such duty exists. The attack here unequivocally is made upon the constitutionality of the Bankruptcy Act insofar as it vests solely in the trustee the right to transfer assets of a bankrupt estate immediately upon adjudication and without regard to the good faith of a bank in honoring, after adjudication, checks drawn by the bankrupt against a bank account representing an asset of the bankrupt estate.[1]

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1. Collier comments specifically that "Deposits in a bank to the credit of a bankrupt pass to the trustee as assets of the estate. Thus,

A. UNDER PRESENT STATUTORY RULES, LACK OF NOTICE IS NO DEFENSE TO THE BANK.

Petitioner argues that since it had no notice of the bankruptcy proceedings, its payment of the bankrupt's check upon presentment by Eureka Fisheries fell within the judicial doctrine exempting certain good faith, post-bankruptcy transactions from the trustee's assertion of a prior right under Section 70a of the Bankruptcy Act. (Petitioner's Brief, pp. 19-24.) Petitioner refers to the "protected transaction" doctrine that developed in the cases prior to the adoption of the Bankruptcy Act of 1938. (52 Stat. 840 (1938), 11 U.S.C. § 1 *et seq.*)

As an abstract matter, there is merit in Petitioner's argument that the "protected transaction" doctrine should apply in this case. The fact is that in 1938 Congress codified the "protected transaction" doctrine in Section 70d. As so codified, the doctrine applies only to post-bankruptcy transactions occurring either (1) before adjudication or (2) before a receiver takes possession of the bankrupt's property, which ever first occurs. The doctrine does not apply after adjudication as Petitioner here asserts. The present statutory scheme of "protected transactions" is clear and unequivocal; it leaves no room for the exception urged by Petitioner.

The 1938 codification of the "protected transaction" doctrine also invalidates Petitioner's argument (Petitioner's

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where through delay, a check drawn on such a deposit prior to bankruptcy is presented, and paid after bankruptcy, the payee is not entitled to retain the sum received as against the trustee." 4 COLLIER, *op. cit. supra*, Sec. 70.31, pp. 1282-3.

We point out also that the deposit here in question was the result of the collection by the bankrupt after bankruptcy of receivables existing at the time of bankrutpcy, and thus no argument has been made, nor could it be, that the deposit in question consisted of after-acquired property of the bankrupt not vesting in the trustee. See 4 COLLIER, *op. cit. supra*, Sec. 70.09, p. 999.

Brief, p. 23) that pre-1938 "protected transaction" decisions relating to pre-adjudication transactions are currently applicable because of the complementary pre-1938 judicial doctrine that the trustee's title to a bankrupt's assets, although not effective until adjudication, related back to the time a bankruptcy petition was filed.

Notwithstanding the codification of the protected transaction doctrine, Petitioner argues that since adjudication in the case of a voluntary bankruptcy petition became automatic with the 1959 amendment of Section 18f of the Bankruptcy Act (73 Stat. 109 (1959), 11 U.S.C. § 41 (f)), Section 70d no longer applies in voluntary bankruptcy cases, and, therefore, that the pre-1938 case law should be reinstated to provide protection to the bank in the present situation. (Petitioner's Brief, pp. 16-18.)

Nothing in the legislative history of Section 18f supports Petitioner's view. Furthermore, reinstatement of the doctrine in voluntary bankruptcy cases would merely serve to reinstate the confusion that existed prior to 1938 and which Congress attempted to remedy by its adoption of Section 70d.

Petitioner's argument also ignores the fact that the automatic adjudication amendment of 1959 had no necessary relationship to the timing of the adjudication in voluntary cases. Under the pre-1959 statute, adjudication was made on application to the district judge, but the application could be made immediately upon the filing of the voluntary petition. (52 Stat. 851 (1938), as amended. See 1964 Bankruptcy Act, comment to § 18f (Collier Pamphlet Ed.). See also *New York County Nat'l Bank v. Massey*, 192 U.S. 138 (1904).)[2]

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2. Even in the case of an involuntary petition, no greater notoriety is given to the fact of adjudication or the appointment of a receiver than occurs when a voluntary petition is filed.

Moreover, nothing on the face of Section 70d indicates that it was intended by Congress to apply exclusively to cases involving involuntary petitions in bankruptcy. The legislative history of Section 70d is directly to the contrary. In his testimony before the House Committee considering the Chandler Bill, Professor James A. McLaughlin, one of the primary draftsmen of the bill, expressly recognized that the question of the trustees' title between the petition and adjudication was a matter of concern in both voluntary and involuntary cases. (Hearings on H.R. 6439, H.R. 8046 Before the House Committee on the Judiciary, 75th Cong., 1st Sess. 210 (1937). See also, Hearings, *op. cit. supra,* pp. 12, 211-12.)

B. THE "NEGOTIABILITY PROVISO" OF BANKRUPTCY ACT SECTION 70d (5) IS NOT APPLICABLE HERE BECAUSE PETITIONER WAS A DRAWEE BANK RATHER THAN A HOLDER OF NEGOTIABLE INSTRUMENTS.

Petitioner here, as did the District Court in *Rosenthal v. Guaranty Bank & Trust Co.,* 139 F. Supp. 730 (W.D. La. 1956), relies heavily upon the proviso contained in Section 70d (5) of the Bankruptcy Act: "That nothing in this Act shall impair the negotiability of currency or negotiable instruments." The court in *Rosenthal* held that because of the "negotiability proviso," a bank was not liable to the trustee when, after the approval of the bankrupt's petition for reorganization (which the court ruled was the equivalent of adjudication for purposes of Section 70d of the Bankruptcy Act (139 F. Supp. at 736)), the bank, in good faith, in the regular course of business, and without actual knowledge of bankruptcy, honored the bankrupt's checks drawn prior to the filing of the petition.

The *Rosenthal* application of the "negotiability" proviso has been severly criticized. For example, Collier comments:

> ". . . a good deal more is read into the proviso of clause (5) by the court in *Rosenthal* . . . than was in-

> tended by the draftsmen. . . . [The court's] emphasis on the bank's good faith seems misplaced; good faith is relevant under § 70d (2) but that clause applies only to the transactions anterior to adjudication. . . . To charge a depository bank with liability for cashing checks of its depositor after his adjudication does not impair the negotiability of the checks. Delivery of a check to the drawee bank for payment is not negotiation." 4 COLLIER, *op. cit. supra,* Sec. 70.68 p. 1502-03 n. 3.

See also Seligson, *Creditors' Rights,* 32 N.Y.U.L. REV. 708, 729-31 (1957); Note, 64 HARV. L. REV. 958, 958 (1951).

"Negotiability" is not defined in the Bankruptcy Act. The question is thus one of state law. (See *Erie R.R. v. Tompkins,* 304 U.S. 64 (1938).) Former Section 3111 of the California Civil Code (Cal. Stats. 1917, c. 751, p. 1538 § 1; Repealed January 1, 1965, Cal. Stats. 1963, c. 819, p. 1997, § 2) provided that:

> "An instrument is negotiated when it is transferred from one person to another in such manner as to constitute the transferee the holder thereof. If payable to bearer it is negotiated by delivery; if payable to order it is negotiated by the endorsement of the holder completed by delivery."

The current California statutory definition is contained in Section 3202 (1), California Uniform Commercial Code:

> "Negotiation is the transfer of an instrument in such form that the transferee becomes a holder. If the instrument is payable to order it is negotiated by delivery with any necessary indorsement; if payable to bearer it is negotiated by delivery."

The California Supreme Court in *Wells Fargo Bank v. Bank of Italy,* 214 Cal. 156, 4 P.2d 781 (1931), ruled that a drawee bank paying an instrument is not a transferee of title since the last holder's endorsement does not trans-

fer the check but converts it into a voucher and thus that the drawee does not become a holder. More recently, the California District Court of Appeal, in the case of *Shammas v. Boyett,* 114 Cal.App. 2d 139, 249 P.2d 880 (1952), said

> ". . . it would seem fairly obvious that a drawee of a draft or bill of exchange who accepts and pays the same upon presentation does not thereby become a holder in due course of the instrument as that term is employed in the law of negotiable instruments. And the authorities uniformly so declare." [Citing state court decisions from Massachusetts, North Carolina, Ohio, Texas and Tennessee, and a United States District Court decision from the Southern District of Illinois.] 114 Cal.App. 2d at 144.

In view of the foregoing, Petitioner's reliance on *Rosenthal* is not persuasive. Petitioner was not a holder of a negotiable instrument; it was a drawee bank charging the checks of the deposits of its bankrupt depositor. The "negotiability" proviso has no bearing.

C. IT IS NO DEFENSE TO THE BANK THAT THIRD PARTIES MAY SHARE THE BANK'S RESPONSIBILITY FOR THE LOSS OF ASSETS.

Petitioner and the California Bankers Association urge that Respondent should be limited to a recovery from the payee of the checks. (Petitioner's Brief, pp. 25-26; Amicus Brief, pp. 9-12.) At this point, insofar as Respondent is concerned, the question is academic because Respondent already has fully recovered from the payee. The Bankruptcy Act, however, does not require such a rule. The focus of Section 70d (5) is on the transfer of assets of a bankrupt estate. A rule that a trustee may recover only from one benefited by the transfer or presently in possession of the fruits of the transfer would seriously limit the trustee's right of recovery. Such a limitation is conspicuously absent

from the provisions of Section 70. By analogy to common law conversion rules, neither the transferor's innocence nor the fact that he no longer has the property is or should be a defense. (See *Poggi v. Scott,* 167 Cal. 372, 139 Pac. 815 (1914); PROSSER, TORTS § 15, pp. 83, 87-88, 98 (3d ed. 1964).) The trustee ought to be entitled to recover from any transferor or transferee. Any other policy would be inconsistent with the scheme of Section 70 which is to permit the speedy and orderly collection of assets of bankrupt estates.

II. Section 70d of the Bankruptcy Act by Invalidating Post-Adjudication Transfers of Assets of Bankrupt Estates Without Regard to the Transferor's Knowledge of Bankruptcy Does Not Deprive the Transferor of Its Property Without Due Process of Law.

Petitioner asserts that these proceedings have deprived it of its property without due process of law. A review of the cases cited in Petitioner's brief, at pages 11-14, reveals that each deals with an entirely distinct problem from that faced by Petitioner herein. The main concern in Petitioner's authorities was whether adequate notice was given of *litigation* adjudicating the rights of parties to the litigation. (*Schroeder v. New York,* 371 U.S. 208 (1962); *Covey v. Somers,* 351 U.S. 141 (1956); *New York v. New York, N.H. & H.R.R.,* 344 U.S. 293 (1953); *Walker v. Hutchinson,* 352 U.S. 112 (1950); *Mullane v. Central Hanover Bank,* 339 U.S. 306 (1949); *Wuchter v. Pizzutti,* 276 U.S. 13 (1928); *Hanover Nat'l Bank v. Moyses,* 186 U.S. 181 (1902).) In none of the foregoing cases did this Court rule that notice to all concerned was prerequisite to the *creation* of legal rights and obligations; notice was required in each case to assure the parties their opportunity for a day in Court in connection with the judicial determination of rights and liabilities. Petitioner herein has had its day in court.

Moreover, *Hanover Nat'l Bank vs. Moyses,* 186 U. S. 181 (1902) cited in Petitioner's brief, at page 11, indicates quite clearly that actual notice is not required to validate bankruptcy proceedings but only such notice as the nature of the proceeding admits. 186 U. S. at 192. Appellant goes too far in stretching this Court's opinion in *Moyses* (which discussed at length the problems inherent in notifying a bankrupt's creditors) into one standing for the proposition that the rights and obligations of a debtor of the bankrupt (apart from the judicial enforcement of those rights and obligations) as a matter of constitutional law cannot be altered until he is notified of the bankruptcy. As a matter of fact, this Court in *Moyses* expressly rejected the due process argument of appellant therein based on inadequate notice saying:

> "Congress may prescribe any regulations concerning discharge in bankruptcy that are not so grossly unreasonable as to be incompatible with fundamental law, and we cannot find anything in this act on that subject which would justify us in overthrowing its action." 186 U. S. at 192.

Louisville Joint Stock Bank v. Radford, 295 U.S. 555 (1935) cited by Petitioner at page 11, involved a legislative attempt to vest insolvent farmers with the right to use the property of others without compensation. No such problem is presented herein because the only assets involved under Section 70d are those belonging to bankrupt estates.

Two of Petitioner's cases, both decided before 1938, simply applied the protected transaction doctrine more broadly than now permitted under Section 70d. (*Frederick v. Fidelity Mut. L. Ins. Co.,* 256 U.S. 395 (1921); *Jones v. Springer,* 226 U.S. 148 (1912).)

Lambert v. California, 355 U.S. 225 (1957) cited in Petitioner's brief, at pages 12-13, is distinguishable because the statute there held unconstitutional on due process grounds, imposed criminal liability not for an affirmative act, but for the failure of a convicted felon to register when the registrant did not know of the registration requirement, and the state had not proved the probability of such knowledge. The Bankruptcy Act creates an obvious risk for the bank quite different from the risk faced by Mr. Lambert. The bank assumed the risk posed by Section 70d.

While Congress cannot ride roughshod over the property rights of those dealing in good faith with bankrupts, Congress certainly may enact legislation balancing conflicting legislative objectives. The history of the development of Section 70d demonstrates that Congress carefully balanced the property rights of those dealing in good faith with bankrupts against the desirability of speedy and orderly administration of bankrupt estates. As evidence thereof, Respondent respectfully refers the Court to the excellent historical analysis contained in 4 COLLIER, *op. cit., supra,* Sections 70.66 and 70.67, pp. 1494.26-1501, inclusive:

> "Prior to the enactment of § 70d as a part of the 1938 Act, there was no statutory law with respect to protected transactions in bankruptcy. Judge-made law, compelled by considerations of justice and equity, frequently moved to protect those whose bona fides in dealing with the bankrupt after bankruptcy were clear. But, as demonstrated hereafter, the situation was fraught with an uncertainty which might have delighted a disciple of the functionalist school of legal philosophy, but which held only the Damocles sword of possible economic loss suspended over those engaged in ordinary commercial pursuits. *The Act of 1938 brought an end to this, and the definitive standards of*

§70d supplanted the nebulous vagaries of the prior law. The statutory innovation thus introduced was largely the result of the impetus furnished by one man —Professor James A. McLaughlin of Harvard University, whose article in the Harvard Law Review in 1927 urged some provision for protected transactions along the lines of the English Act. As there stated by Professor McLaughlin and later repeated by him in the *Analysis of H.R. 12889,* the situation was "conducive to confusion and uncertainty, with potentialities for argument, 'bluffing', litigation, expense and delay.'

• • •

"As previously stated in the treatise, the courts prior to 1938 were faced with two contradictory concepts. On the one hand, despite the inconsistent language of § 70a and the lack of definite statement in other provisions of the Act, the filing of the petition was held to be a *caveat* to the whole world, and in effect an attachment and injunction. This proposition was an essential prop to the bankruptcy court's assertion of jurisdiction and power in preventing the dissipation and attachment of the assets of the estate, in determining the rights of claimants under the various provisions of the Act, in fixing the right of set-off against the estate, in enjoining non-bankruptcy proceedings that interfered with the bankruptcy administration, and generally in adjudicating the very nature and extent of the bankruptcy court's exclusive control. On the other hand, the courts were often impelled to make exceptions to the doctrine where its application would work a hardship on an innocent party who, following the inception of bankruptcy, dealt with the bankrupt on a bona fide basis for a present consideration. The concept that the filing of the petition was a sort of *lis pendens* was probably justifiable and proper in the instances just previously enumerated, but where innocent parties were concerned, it was recognized that as a practical matter the mere filing of the petition gave rise to no

actual notice that would put such persons on guard. *These propositions, of course were inherently inconsistent, and whether the one or the other would prevail in a close case was always a matter of conjecture.* Nor was the confusion improved by the gradual and parallel evolvement of the 'relation back' doctrine, which served to rationalize the introductory portion of § 70a with the provisions of § 70a(5) and fixed the date of filing the petition as the date of cleavage with respect to the trustee's title. As a matter of fact, the former statement in the introductory portion of § 70a that appeared to fix the trustee's title as of the date of adjudication was seized upon by some courts to justify the protection of a particular transaction, even though in other situations the time of filing came to be regarded as the determinative date.

"From this development, however, certain instances could be singled out where it was possible to predict that the transaction, even if effected after bankruptcy, would be protected from invalidation. Thus it was held that an alleged bankrupt, acting in good faith, was entitled to conduct his business, enter into legitimate contracts in connection therewith and utilize his funds in paying the expenses of operation prior to his adjudication or until such time as a custodian or receiver was appointed to take charge of the estate. Payments of funds of the bankrupt, without notice of bankruptcy and in the usual course of business—as by a bank or an insurance company—, were also protected *prior to* adjudication or the appointment of some officer to have preliminary custody or possession of the estate. Of course, if the transaction were actually fraudulent or amounted to a preference of a creditor, whether the creditor was innocent or not, it could not be sustained. *And it was undisputed that after an adjudication, in bankruptcy, all transfers of the bankrupt's property both by or to innocent parties were nonetheless invalid.* It was said that an adjudication was notice to all the world.

"Yet despite these instances, there remained considerable uncertainty as to how far and when the theory of protected transactions could be implemented. The courts themselves were cautious and somewhat doubtful in their language, and as Professor McLaughlin so aptly pointed out, the situation was fraught with undesirable possibilities that demanded correction. . . .

"It was admitted by the proponents of § 70d that its enactment as a part of the 1938 Act would not tend to increase subsequent dividends to creditors of bankrupt estates. But, as pointed out by Professor McLaughlin, it was possible to go too far the other way in cutting off all rights or claims as of the date of bankruptcy. Despite the temptation to use a picturesque metaphor, the courts prior to 1938 had been prone to conclude that for some purposes, at least, one who was petitioned against was neither civilly nor economically dead. Section 70d recognizes this practical viewpoint and has the added virtue of defining . . . the exact limits under which certain specified transactions will be protected. *Beyond those limits the courts are no longer free to go.*

"*The theory of protected transactions as enunciated by § 70d creates, of course, an exception to the general rule, now firmly fixed by the Act, that the time of filing the petition is the date of cleavage in bankruptcy.* Thus the operation of the mere filing of the petition as a *caveat* must give way to this statutory qualification. The draftsmen of the 1938 Act were consistent, however, in their regard for protected transactions. The contemporaneous adoption of § 63b has made possible the filing of claims by those who contract on a bona fide basis with an involuntary bankrupt before adjudication or the appointment of a receiver.

"*But it must be kept in mind that § 70d . . . defines the full extent to which bona fide transactions with the bankrupt, after bankruptcy, will be protected. Subject to the exceptions thus created, the bankruptcy petition*

is still a caveat and persons dealing with the bankrupt thereafter do so at their own peril. (Emphasis supplied; footnotes omitted.)

In his 1937 testimony before the Chandler Committee, Professor McLaughlin analyzed the reasons for the adoption of Section 70d as follows:

"The trustee's title is in an unsatisfactory state . . . with reference to the time when it accrues. The Act of 1898 states that he gets title as of the adjudication, but makes no express provision for the general protection of the bankrupt estate in the interim between the petition and the adjudication. This gap has necessarily been supplied by the courts, but in an unsystematic manner, which at times seems almost disingenous. The Supreme Court in *Mueller v. Nugent* declared that 'a petition in bankruptcy is a *caveat* to all the world, and in effect an attachment and injunction.' This statement may seem on its face to be a potent source of litigation. Any suspicion to this effect is not diminished by the fact that it has been cited over thirty times by the Supreme Court and more than three hundred times by the lower federal courts. Few, if any, bankruptcy cases have been cited as frequently, and indeed there cannot be many Twentieth Century cases in any field which have been more frequently so noticed. The above quoted *dictum* has been the life of the entire party. It has been entertained in almost every conceivable way, being applied according to its face value or distinguished as convenience or common sense dictates. Mr. Justice Holmes said the statement 'must be taken with reference to the facts before the court and not as applicable to all intents and purposes.' He cited with approval a passage where Sanborn, J., referred to 'later decisions of the Supreme Court adjudging that this statement applies only to parties who have no substantial claim of a lien upon or a title to the property of the bankrupt, and that,

against those who have such claims . . . . when the petition . . . . is filed, ... its filing is neither a *caveat* or an attachment and that it creates no lien. . . . .' Circuit Judge Ward, upholding a decision in favor of a bank honoring a check of the bankrupt between the petition and the adjudication, said, 'whatever else the remark may mean, it cannot mean, in contradiction to the express provision of the Act, that the title of the bankrupt shall vest in the trustee as of the time of filing of the petition.' However, even this apparently safe statement is far from the truth, for it is stated that 'broadly speaking the adjudication when made relates back to the commencement of bankruptcy proceedings.' The fact is that the theory of a date of cleavage as of which the assets and liabilities of the estate are adjusted is almost indispensable to the conduct of bankruptcy administration. The Bankruptcy Act of 1898 is clearly constructed with primary reference to the filing of the petition as the date of cleavage. As we have seen, the failure to prohibit transactions detrimental to the estate after the petition suggests the assumption that the property is *in custodia legis,* at least 'for certain purposes,' after the petition. Furthermore, claims are made provable or not depending upon their existence in some form at the date of the petition. Apart from unimportant exceptions proposed by the Chandler Bill the bankrupt has unqualified title to the property he acquires after the date of the petition. Upon the whole, it seems fair to say that, whatever this much discussed *dictum* may mean, the Bankruptcy Act of 1898 really means precisely that 'the title of the bankrupt shall vest in the trustee at the time of the petition,' 'in contradiction to the express provision' found in one clause of the Act.

"The only trouble with this theory is that it discloses a very serious gap in the Act of 1898 in that there is no reference to transactions to be protected after

> the date of the petition. The simplest solution is to give the trustee title from the petition and expressly provide for the type of subsequent transactions to be protected. The Chandler Bill endeavors to give the courts such a clear statutory basis (in lieu of a crazy quilt of contradictory judicial statements) with which to continue to work out a reasonable system for balancing the conflicting interests during the term between the commencement of the proceedings and the commencement of the actual administration when the receiver or trustee moves to reduce the assets to his possession." Hearings on H.R. 6439, H.R. 8046 Before the House Committee on the Judiciary, 75th Cong., 1st Sess. 211-12 (1937).[3]

The foregoing historical record has been given judicial recognition in the Fourth Circuit decision of *Lake v. New York Life Ins. Co.*, 218 F.2d 394 (1954), where the Court of Appeals concludes, after reviewing the factors discussed above:

> "It is obvious that the intent of . . . [Section 70d] . . . is to invalidate transactions not granted specific protection under the Act and thus put to an end the confusion theretofore existing in the decisions. There is almost always some injustice or hardship which attends transactions occurring after the filing of a petition in bankruptcy between the bankrupt, acting wrongfully, and an innocent third person, because the loss must fall either upon the third person or upon the creditors of the bankrupt. Whether the line which has been drawn is the best possible solution of the problem is not for the courts to say. The line has in fact been drawn by competent authority and it is no longer

3. Professor McLaughlin was reading from his article "Aspects of the Chandler Bill to Amend the Bankruptcy Act," published in the University of Chicago Law Review shortly before his appearance before the Chandler Committee. 4 U. CHI. L. REV. 369, 381-83 (1937).

necessary for the courts to make the attempt, which has not been conspicuously successful in the past, to decide cases on the facts as they arise and to draw a fine distinction between transactions which should be protected and those which should not. . . ." (218 F.2d at 399.)

A great deal has been said in Petitioner's brief about the injustice of a rule that a bank is not protected on payments made by it of funds belonging to the bankrupt's estate subsequent to the filing of a voluntary petition in bankruptcy where the bank has no actual notice of the bankruptcy.

Any bank must certainly be charged with knowledge of the possibility of bankruptcy of any of its depositors. Some protection to the bank would be offered in the daily scanning of legal publications containing notices of local adjudications. We believe Petitioner exaggerates when it says "To be fully protected the bank would have to keep itself advised momentarily of every bankruptcy filing in every district in the country." (Petitioner's Brief, p. 14.) Common experience indicates that depositors tend to bank near their commercial activity. Bankruptcy petitions normally will be filed in the district in which a depositor resides or has his principal place of business. (Bankruptcy Act § 2a (1), 52 Stat. 842 (1938), 11 U.S.C. § 11(a).)

The impact upon banks of the rule urged by Respondent is likely to be reduced further by the likelihood that, exactly as happened here, the payee of the check will pay the trustee, and even if the bank pays initially it would have a cause of action against the payee since the bank paid under mistake of fact and the payee was unjustly enriched. See RESTATEMENT, RESTITUTION, §§ 9, 16, 23 (1937); *National Bank of California v. Miner*, 167 Cal. 532, 140 Pac.

27 (1914); *American Oil Service v. Hope Oil Co.*, 233 Cal. App. 2d 822, 830-31, 44 Cal. Rptr. 60, 65-66 (1965); *Burckard v. Smith*, 80 Cal. App. 104 (1926).

On the other hand, Congress was fully conscious of the timing problem faced by trustees. Normally there is an interval between the filing of a voluntary bankruptcy petition and appointment and qualification of a trustee or receiver, and there necessarily is a second gap before the trustee or receiver can notify the bankrupt's debtors of the appointment. Here the interval between appointment of the receiver and the mailing of notice to the bank was two days (R. 1, 44, 45-46), not an unreasonable time when it is remembered that the bankrupt's balance at the bank at the time of adjudication was a nominal $195.54. (R. 7.) The interval will vary depending upon the accuracy and completeness of the information given by the debtor as well as the trustee's ability to find the debtor and the debtor's proximity.

Regardless, Congress did not provide in Section 70a that the trustee shall be vested with title upon giving notice of bankruptcy to those in possession of assets of the bankrupt estate. Congress provided that title shall vest in the trustee "by operation of law . . . as of the date of the filing of a petition in bankruptcy." The solution achieved in Section 70d is not arbitrary. Since the statutory solution reasonably serves conflicting goals, the statute does not infringe constitutional rights of due process. *Hanover Nat'l Bank v. Moyses*, 186 U. S. 181 (1902). As one writer commented:

> ". . . much of the usual routine of due process may be clipped short where due and speedy administration of the affairs of an insolvent is the objective and a liquidation and settlement of his affairs is of paramount

practical importance." 1 REMINGTON, BANKRUPTCY, Section 11, p. 23 (1950).

If the rule is too harsh, Petitioner should direct its criticism to Congress.

III. The Decision of the Court of Appeals Does Not Require Petitioner to Pay the Same Debt Twice.

A. PETITIONER'S CLAIM THAT IT WILL BE REQUIRED TO PAY TWICE IS OBVIOUSLY SPECULATIVE.

Petitioner's claim that it may be required to pay twice is based upon the reasoning that since the referee held Petitioner and Eureka Fisheries jointly liable to Respondent for the sum of $2,312.82, and since Eureka Fisheries paid said sum to Respondent and demanded contribution from Petitioner, Eureka Fisheries thereby became entitled "to the remedy of execution to recover from the bank one-half the amount Eureka Fisheries paid on the joint judgment." (Petitioner's Brief, p. 4.) Petitioner implies that the remedy of execution is immediately available to Eureka Fisheries "without the necessity of further proceedings." (Petitioner's Brief, p. 5, footnote 1.)

Whether the remedy of execution is immediately available to Eureka Fisheries was the subject of supplemental briefs requested by the Court of Appeals below (R. 104), and in its opinion the Court of Appeals expressly reserved opinion as to whether Petitioner will have to pay any part of the obligation satisfied by Eureka Fisheries. (R. 116, footnote 12.)

Under California law, a claim for contribution is not enforceable by writ of execution as Petitioner contends, but rather must be enforced (1) by separate legal action or (2) upon noticed motion in the same action. (See, for example, *Backer v. Grummett,* 39 Cal. App. 101, 178 Pac.

312 (1918); *Stowers v. Fletcher,* 84 Cal. App. 2d Supp. 845, 848 (1948).

If and when Eureka Fisheries asserts its contribution claim the bank may raise the defense that in paying the trustee pursuant to the joint judgment, Eureka Fisheries merely was disgorging a payment by which it had been unjustly enriched, and which was made to it by the bank under mistake of fact. (*Cf.* cases cited at pages 20-21 above.)

B. THE COURT OF APPEALS' DECISION DOES NOT HOLD PETITIONER RESPONSIBLE FOR A DEBT THAT HAS BEEN PAID HERETOFORE.

Although the lower courts held Petitioner jointly accountable with Eureka Fisheries to Respondent trustee in bankruptcy for assets of the bankrupt estate (R. 48, 99-100) and although the Court of Appeals sustained that judgment over Petitioner's objection (R. 105-116), no decision herein requires Petitioner to pay both the trustee and Eureka Fisheries. Petitioner's payment to Eureka Fisheries was made voluntarily and not in satisfaction of a legal obligation, but under a mistake of fact. The legal relationship of the parties changed by operation of law at the moment the bankruptcy petition was filed. Thereafter, although the bank remained under the mistaken impression that it was obligated to pay as directed by its bankrupt depositor, it had no obligation to pay. The bank's only obligation was to pay the trustee, and payment to a third party violated the express mandate of Section 70 of the Bankruptcy Act.

Brief comment is necessary at this point concerning the argument of the California Bankers Association (Amicus Brief, pp. 3-8) that the bank's contractual obligation to pay Eureka Fisheries could be terminated only by timely stop payment notice from Respondent. The argument is based

upon the erroneous assumption that at the time the bankrupt's orders for payment were delivered to the bank the bankrupt still had the right to order payment against its account. Section 70a is clear that the bankrupt's right to order payment against its account terminated on the date the bankruptcy petition was filed, in this case six days before the bank received the bankrupt's checks. (R. 44, 46.)

C. EUREKA FISHERIES' CONTRIBUTION CLAIM IS INDEPENDENT OF THE TRUSTEE'S CLAIM AGAINST THE BANK AND, THEREFORE, NO PROBLEM OF OVERLAPPING JURISDICTION EXISTS.

The question of Eureka Fisheries' alleged right to contribution has no bearing on the bankruptcy question, for it is recognized under California law that the right to contribution constitutes a new and distinct obligation in favor of one satisfying a joint judgment. (See, for example, *Pacific Freight Lines v. Pioneer Express Co.*, 39 Cal.App 2d 609, 103 P.2d 1056 (1940).

Section 2 of the Bankruptcy Act (52 Stat. 842 (1938), as amended, 11 U.S.C. § 11) demonstrates on its face a Congressional intent to limit the jurisdiction of bankruptcy courts to issues necessary to the preservation and collection of bankrupt estates. Nothing therein suggests a broad jurisdictional grant to determine collateral disputes having no effect on the assets of bankrupt estates. (See, for example, subsections 2a(2), 2a(3), 2a(5), 2a(15).)[4]

Because the contribution claim is independent, Petitioner's problem of potential liability to Eureka Fisheries

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4. Respondent notes also that, apart from bankruptcy, Eureka Fisheries' contribution claim presents no issue cognizable in federal court for the reason that there has been no showing that the parties to the dispute are of diverse citizenship (28 U.S.C. § 1332); the claim presents no controversy arising under the Constitution, laws or treaties of the United States (28 U.S.C. § 1331); and the amount of the claim, that is $2,312.82, is below the jurisdictional minimum of federal courts (28 U.S.C. §§ 1331, 1332).

is quite different from the problems considered by this Court in the cases cited in Petitioner's Brief at page 15.

In *Western Union v. Pennsylvania,* 368 U. S. 71 (1961), this Court was faced with conflicting claims to a single fund by several states. No single state court could effectively adjudicate a claim asserted by a sister state. The problem was the practical one of finding a forum with jurisdiction that extended throughout all states concerned, and such a forum was found in the United States Supreme Court. In our case, the comparable forum for the resolution of claims to the assets of bankrupt estates is found in bankruptcy proceedings and the resolution of the contribution claim is unnecessary to the resolution of the bankruptcy proceedings.

Harris vs. Balk, 198 U. S. 215 (1905), also dealt with the problem of conflicting jurisdiction and the possibility that payment of an obligation in one forum would not effectively protect an obligor from re-assertion of the obligation in a second forum. Petitioner here has made no showing that it might have been held liable to either its depositor or the payee on the depositor's check had it refused to honor a check drawn on the account of its bankrupt depositor.

Huron Holding Corp. v. Lincoln Mine Operating Co., 312 U. S. 183 (1941), is also distinguishable. This Court was there concerned with the assertion of a single obligation in both state and federal court proceedings.

For the foregoing reasons, Respondent believes that there is no basis for Petitioner's claim that it has been or will be required to pay the same debt twice or that the judgment infringes constitutional standards defined in *Western Union, Harris, or Huron Holding Corp.*

CONCLUSION

For the foregoing reasons, Respondent respectfully submits that the judgment of the Court of Appeals for the Ninth Circuit should be affirmed.

Respectfully submitted,

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September 12, 1966

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In the Supreme Court
OF THE
United States

OCTOBER TERM, 1966

No. 63

BANK OF MARIN,
Petitioner,
vs.
JOHN M. ENGLAND, Trustee in Bankruptcy,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

REPLY BRIEF FOR THE PETITIONER

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ARGUMENT

The trustee relies upon two similar arguments to refute the bank's contention that the Court of Appeals' decision requires the bank to pay the same debt twice. Not only are both arguments unsupported by authority, but they fail to deal with the issue involved. (Respondent's Brief, pp. 4, 22, 23, 24.)

I

THE TRUSTEE'S CONTENTION THAT THE BANK'S PAYMENT WAS MADE UNDER MISTAKE IS GROUNDLESS SINCE THE VERY PREMISE UPON WHICH IT IS BASED IS A FAVORABLE DECISION BY THIS COURT ON THE ISSUE PRESENTED.

The trustee contends that since the legal relationship between the bank and its depositor changed by operation of law at the moment the bankruptcy petition was filed, the bank's payment to Eureka Fisheries was not made in satisfaction of a legal obligation, but was made under a mistake of fact. Therefore, the trustee reasons, the bank is being compelled to pay the same debt only once. (Respondent's Brief, p. 23.)

The trustee's argument is based upon the premise that when the checks were presented to the bank for payment, the bank's sole obligation was to the trustee. It is only by making such an assumption that the trustee can claim that payment by the bank was made under mistake. Whether the bank was so obligated is the very issue to be decided. Accordingly, the trustee's contention that the bank is not being compelled to pay the same debt twice is groundless, since it is founded upon the presumption of a favorable decision by this Court.

II

THE BANK'S CONTENTION THAT THE COURT OF APPEALS' DECISION REQUIRES IT TO SATISFY THE SAME DEBT TWICE IS NOT SPECULATIVE.

The trustee argues that the bank's claim that it will have to pay twice is speculative since the bank

can assert that its payment to Eureka Fisheries was made under mistake and therefore, the bank may have a defense to Eureka Fisheries' contribution claim. (Respondent's Brief, pp. 22, 27.) This contention is without merit for three reasons.

(a) Whether the Bank May Have a Defense to the Contribution Claim Is Immaterial.

Whether or not the bank has a possible defense to Eureka Fisheries' contribution claim has nothing to do with double payment. The bank's contention is that by holding it jointly liable with the payee for the sums it paid in honoring the checks, the Court of Appeals is requiring it to satisfy the same obligation twice. The fact that the bank may or may not have a defense to enforcement of contribution by its joint judgment debtor does not alter the effect of the original judgment which imposed liability against the bank.

(b) The Nature of the Right to Contribution in California Is Such That a Claim That Payment Was Made Under Mistake Cannot Constitute a Defense.

The availability of contribution is determined by state law. *Kennedy v. Pennsylvania Railroad Company* (2nd Cir. 1960) 282 F.2d 705; *Smith v. Whitmore* (3rd Cir. 1959) 270 F.2d 741. In this regard, California law provides that where one of several joint judgment debtors pays more than his proportionate share of the judgment he is entitled to obtain contribution from those jointly liable with him. California Civil Code Section 1432; *Woolley v. Seijo,* 224 Cal.App.2d 615, 36 Cal.Rptr. 762 (1964); *Tucker*

v. Nicholson, 12 C.2d 427, 84 P.2d 1045 (1938). This may be accomplished in any one of three ways.

California Code of Civil Procedure Section 709 provides a summary method whereby a joint judgment debtor may enforce the judgment itself against his co-debtors without the necessity of bringing an action. *McIntosh v. Funge,* 128 Cal. App. 70, 16 P.2d 1006 (1932); *Blake v. Arp,* 48 Cal.App. 715, 192 Pac. 452 (1920); *Forsythe v. Los Angeles Railway Company,* 149 Cal. 569, 87 Pac. 24 (1906). The customary procedure is to notice a motion for issuance of a writ of execution. Upon an appropriate showing of the amount of the judgment paid and the proportionate share that should have been paid by the joint judgment debtors, a writ of execution will be issued by the Court. *Stowers v. Fletcher,* 84 Cal.App.2d Supp. 845, 190 P.2d 338 (1948); *Davis v. Heimbach,* 75 Cal. 261, 17 Pac. 199 (1888).[1]

As an alternative to proceeding under California Code of Civil Procedure Section 709, a joint judgment debtor, upon paying the entire judgment, may take an assignment of the judgment and obtain execution against the co-judgment debtors for their proportionate share. *Tucker v. Nicholson,* 12 C.2d 427, 84 P.2d 1045 (1938). Again, the customary procedure

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[1]At the request of the Court of Appeals for the Ninth Circuit, Eureka Fisheries filed a memorandum describing its position with respect to its contribution claim. In that memorandum Eureka Fisheries stated that it intended to proceed against the Bank of Marin pursuant to California Code of Civil Procedure Section 709, but that it was voluntarily withholding enforcing its right to contribution pending final determination of this litigation in the appellate courts.

is to proceed pursuant to a noticed motion for issuance of a writ of execution. The same showing is made as under Code of Civil Procedure Section 709.

Whether the debtor proceeds under California Code of Civil Procedure Section 709, or by taking an assignment of the judgment, the judgment is kept alive, to be used by the debtor to recover from his co-obligors the proportion they should pay. *Tucker v. Nicholson,* 12 C.2d 427, 430, 84 P.2d 1045 (1938); *Williams v. Reihl,* 127 Cal. 365, 59 Pac. 762 (1899). The claim to contribution is founded upon the judgment itself and not upon any new or distinct obligation. It is not proper to go behind the judgment to ascertain whether the co-obligors were properly held liable.[2] The only issue to be determined is what amount of the joint judgment the moving party has paid and what proportion of the judgment his co-judgment debtors should pay. The contention that the original payment giving rise to the joint judgment was made by mistake cannot properly be asserted as a defense.

In addition to the two summary procedures outlined above, a joint judgment debtor can initiate an independent action against those jointly liable with him to obtain a contribution. *Woolley v. Seijo,* 224 Cal.

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[2]The joint judgment, if not reversed as to the bank, is res judicata on the issues giving rise to the bank's liability. *Estate of Merrill,* 29 C. 2d 520, 175 P.2d 819 (1946). In *Estate of Merrill,* the California Supreme Court held that payment of a joint judgment by one of two joint judgment debtors could not deprive the other joint judgment debtor of his right to an appeal on the merits, since the judgment would become res judicata as to all issues imposing liability.

App.2d 615, 36 Cal.Rptr. 762 (1964); *Pacific Freight Lines v. Pioneer Express Company,* 39 Cal.App.2d 609, 103 P.2d 1056 (1940).

Again, it is highly doubtful that it could be successfully asserted as a defense to a claim to contribution in such a proceeding that the payment giving rise to the original joint judgment was made under mistake. This is particularly true in this action where the nature of the bank's payment to Eureka Fisheries was one of the issues litigated in the bankruptcy court.[3]

(c) The Bank Cannot Assert as a Defense to the Contribution Claim That It Paid Eureka Fisheries Under Mistake.

Eureka Fisheries received the checks that Marin Seafoods drew on the Bank of Marin in good faith for value, and as such was a holder in due course. *Flores v. Wood Specialties, Inc.,* 138 Cal.App.2d 763, 292 P.2d 626 (1956). Under such circumstances, no claim can be made that Eureka Fisheries was unjustly enriched. Therefore, payment by the bank under the facts of this case does not constitute the type of mistake of fact that would permit the bank to recover any funds paid or to defend against a claim asserted by the payee. See: Restatement, Restitution, Sections 14, 33 (1937); California Civil Code Section 3143; (Repealed January 1, 1965, Cal.Stats. 1963 c. 819, p. 1997, sec 2; replaced by California Commercial Code Sections 3413, 3418); cases collected Annot. 114 A.L.R.

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[3]See pages 13 and 22 of the record wherein Eureka Fisheries asserted that payment by the bank was in the nature of an overdraft and therefore only the bank should be held responsible.

382 (1938); *Crocker-Woolworth Bank v. Nevada Bank,* 139 Cal. 564, 73 Pac. 456 (1903).[4]

Dated, San Rafael, California,
October 4, 1966.

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BRYAN R. MCCARTHY,
EDGAR B. WASHBURN,
FREITAS, ALLEN, MCCARTHY & BETTINI,
Counsel for Petitioner.

[4]It can also be argued that payment by the bank was analogous to payment creating an overdraft in the depositor's account. It is well established that a drawee bank which pays an overdraft check to one who presents it in good faith will not be permitted to recover the money so paid even though it was paid by mistake. *Larrus v. First National Bank of San Mateo,* 122 Cal.App.2d 884, 266 P.2d 143 (1954). See cases cited: 15 Calif. Law Rev. 235 at 236 (1927); Brady, "Bank Checks", pp. 358-360 (3rd Ed., 1962).

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SUPREME COURT OF THE UNITED STATES

No. 63.—October Term, 1966.

Bank of Marin, Petitioner, v. John M. England, Trustee in Bankruptcy.	On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit.

[November 21, 1966.]

Mr. Justice Douglas delivered the opinion of the Court.

The question presented by this case is whether a bank which honored checks of a depositor drawn before his bankruptcy but presented for payment after he had filed a voluntary petition in bankruptcy, is liable to the trustee for the amount of the checks paid where the bank had no knowledge or notice of the proceeding. The trustee applied to the referee for a turnover order requiring petitioner bank to pay to the trustee the amount of the checks and in the alternative asking the same relief against the payee. The referee determined that petitioner and the payee were jointly liable to the trustee. The District Court affirmed. Only petitioner appealed and the Court of Appeals affirmed the District Court. 352 F. 2d 186. We granted certiorari because of the importance of the question presented. Cf. *Rosenthal* v. *Guaranty Bank & Trust Co.*, 139 F. Supp. 730; *Mullane* v. *Central Hanover Bank & Trust Co.*, 339 U. S. 306.

I.

We were advised on oral argument that the joint judgment rendered against petitioner bank and the payee of the checks was paid in full by the payee and that at present respondent's sole financial interest in this litigation is protection against imposition of costs under our Rule 57. It is therefore suggested that the case is moot.

We do not agree. Whatever might be the result if costs alone were involved (cf. *Heitmuller* v. *Stokes*, 256 U. S. 359, 362) this case should not be dismissed. We are advised that the payee paid the joint judgment and has filed with the Bankruptcy Court and served on petitioner a demand for contribution from it respecting sums paid in satisfaction of the judgment. Thus petitioner is still subject to a suit because of the original judgment as to its liability. We would, therefore, strain the concepts of mootness if we required petitioner to start all over again when the payee sues it for contribution.

II.

Section 70 (a) of the Bankruptcy Act, 52 Stat. 879, 11 U. S. C. § 110 (a), provides that a trustee in bankruptcy is vested "by operation of law" with the title of the bankrupt as of the date of the filing of the petition to described kinds of property "including rights of action." § 70 (a)(5). But we do not agree with the Court of Appeals that the bankrupt's checking accounts are instantly frozen in the absence of knowledge or notice on the part of the drawee of the bankruptcy. The trustee succeeds only to such rights as the bankrupt possessed; and the trustee is subject to all claims and defenses which might have been asserted against the bankrupt but for the filing of the petition. See *Zartman* v. *First National Bank*, 216 U. S. 134, 138. The relationship of bank and depositor is that of debtor and creditor, founded upon contract. The bank has the right and duty under that contract to honor checks of its depositor properly drawn and presented (*Allen* v. *Bank of America*, 58 Cal. App. 2d 124, 127, 136 P. 2d 345, 347; *Weaver* v. *Bank of America*, 59 Cal. 2d 428, 431, 380 P. 2d 644, 647; and see *Anderson National Bank* v. *Luckett*, 321 U. S. 233) absent a revocation that gives the bank notice prior to the time the checks are accepted or paid by the bank.

See *Hiroshima* v. *Bank of Italy*, 78 Cal. App. 362, 369, 248 P. 947, 950. The Court of Appeals held that the bankruptcy of a drawer operates without more as a revocation of the drawee's authority. 352 F. 2d, at 191. But that doctrine is a harsh one that runs against the grain of our decisions requiring notice before a person is deprived of property (*Mullane* v. *Central Hanover Bank & Trust Co.*, *supra*, at 314–318; *Walker* v. *City of Hutchinson*, 352 U. S. 112; *Schroeder* v. *City of New York*, 371 U. S. 208), a principle that has been recognized and applied in proceedings under the Bankruptcy Act. *New York* v. *New York, N. H. & H. R. Co.*, 344 U. S. 293, 296–297. The kind of notice required is one "reasonably calculated, under all the circumstances, to apprise the interested parties of the pendency of the action." *Mullane* v. *Central Hanover Trust & Bank Co.*, *supra*, at 314. We cannot say that the act of filing a voluntary petition in bankruptcy *per se* is reasonably calculated to put the bank on notice. Absent revocation by the drawer or his trustee or absent knowledge or notice of the bankruptcy by the bank, the contract between the bank and the drawer remains unaffected by the bankruptcy and the right and duty of the bank to pay duly presented checks remain as before. In such circumstances the trustee acquires no rights in the checking account greater than the bankrupt himself.

Section 70 (d) (5), 52 Stat. 882, 11 U. S. C. § 110 (d) (5), provides, with exceptions not relevant here, that "no transfer by or in behalf of the bankrupt after the date of bankruptcy shall be valid against the trustee." And in case of a voluntary petition (with exceptions not material here) the filing operates as an adjudication. § 18 (f), 73 Stat. 109, 11 U. S. C. § 41 (f). It is therefore argued with force that payment by the drawee of a drawer bankrupt's checks after the date of that filing is a "transfer" within the meaning of § 70 (d) (5).

Yet we do not read these statutory words with the ease of a computer. There is an overriding consideration that equitable principles govern the exercise of bankruptcy jurisdiction. Section 2 (a), 52 Stat. 842, 11 U. S. C. § 11 (a); *Pepper* v. *Litton*, 308 U. S. 295, 304–305; *Securities & Exchange Commission* v. *U. S. Realty & Imp. Co.*, 310 U. S. 434, 455. We have said enough to indicate why it would be inequitable to hold liable a drawee who pays checks of the bankrupt duly drawn but presented after bankruptcy, where no actual revocation of its authority has been made and it has no notice or knowledge of the bankruptcy. The force of § 70 (d)(5) and § 18 (f) can be maintained by imposing liability on the payee of the checks where he has received a voidable preference or other voidable transfer. The payee is a creditor of the bankrupt, and to make him reimburse the trustee is only to deprive him of preferential treatment and to restore him to the category of a general creditor. To permit the trustee under these circumstances to obtain recovery only against the party that benefited from the transaction is to do equity.

Reversed.

SUPREME COURT OF THE UNITED STATES

No. 63.—October Term, 1966.

Bank of Marin, Petitioner, v. John M. England, Trustee in Bankruptcy.	On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit.

[November 21, 1966.]

Mr. Justice Harlan, dissenting.

The Court, in its haste to alleviate an indisputable inequity to the bank, disregards, in my opinion, both the proper principles of statutory construction and the most permanent interests of bankruptcy administration. I must dissent.[1]

The Act itself is unambiguous. Section 70 (a) vests title to the bankrupt's property in the trustee "as of the date of the filing of the petition." 52 Stat. 879, 11 U. S. C. § 110 (a). Section 70 (d) nonetheless sustains bona fide transfers of the property made after filing and "before adjudication or before a receiver takes possession . . . whichever first occurs. . . ." 52 Stat. 881, 11 U. S. C. § 110 (d). Transactions excluded from the shelter of § 70 (d) are, so far as pertinent, within § 70 (d) (5), which provides that "no [such] transfer by or in behalf of the bankrupt . . . shall be valid against the trustee. . . ." 52 Stat. 882, 11 U. S. C. § 110 (d) (5). The adjudication of voluntary petitions results by operation of law from filing. § 18 (f), 73 Stat. 109, 11 U. S. C. § 41 (f).

In the situation before us, the remaining issue is accordingly whether this transfer occurred before or after

[1] Like the Court, I believe that this case is not moot. In addition to what has been said by the majority, compare *Fishgold* v. *Sullivan Drydock & Repair Corp.*, 328 U. S. 275, and *Aeronautical Industrial Dist. Lodge* v. *Campbell*, 337 U. S. 521.

September 26, the day on which Seafoods filed its petition in bankruptcy and was perforce adjudicated bankrupt. I do not understand petitioner to contend, or the Court to suggest that this occurred at a time other than presentment of the checks, October 2. Given the law of California, by which a check is not a *pro tanto* transfer of the drawer's rights until presentment, I cannot see that another moment is possible. California Civil Code § 3265e. California Commercial Code § 3409. In sum, I find it unavoidable that the Act's plain words hold the bank liable to the trustee for the value of its payment on Seafoods' behalf.[2]

I do not suggest that this Court should confine its attention to the unadorned terms of the Bankruptcy Act. Nonetheless, where Congress has pointed so unmistakably in one direction, prudence and simple propriety surely require that we examine carefully the impulses which beckon us to another. The Court explains its resolution of this case by two apparently alternative contentions. I am unpersuaded that either permits us to circumvent the Act's demands.

The Court first intimates, without expressly deciding, that the bank is shielded by its contractual right to a seasonable revocation of its duty to honor checks drawn upon it. The Court vouches for this the doctrine that a trustee in bankruptcy takes rights no wider or more complete than had his bankrupt. It is doubtless true that a trustee is not a bona fide purchaser or encum-

[2] It is true that the negotiability proviso to § 70 (d)(5) has once been held to protect a bank in analogous circumstances. *Rosenthal v. Guaranty Bank and Trust Co.*, 139 F. Supp. 730. The proviso's legislative history throws little light on its intended scope. It appears inapplicable here. First, presentment is not strictly a negotiation. Second and more important, other constructions are more consonant with the balance of § 70 (d). Cf. 70 Harv. L. Rev. 548, 550. 4 Collier, Bankruptcy ¶ 70.68, at 1502n. I do not understand the Court to rely upon the proviso.

brancer, and that he ordinarily assumes the bankrupt's property subject to existing claims, liens, and equities. *Hewit* v. *Berlin Machine Works*, 194 U. S. 296. Unfortunately, these maxims scarcely suffice to decide this case. They are interstitial rules, valid no further than the Act's positive requirements permit. *First National Bank* v. *Staake*, 202 U. S. 141. 4 Collier, Bankruptcy ¶ 70.04, at 954.2. The Act in several respects clothes the trustee in powers denied to his bankrupt: A trustee may thus avoid, although his bankrupt may not, transactions deemed fraudulent under the Act, liens obtained and preferential transfers completed within four months of bankruptcy, and statutory liens within the prohibition of § 67 (c)(2). 4 Collier, Bankruptcy ¶ 70.04, at 957.

The Court does not assert that this transfer is protected by § 70 (d). I understand it instead to concede that, equitable considerations aside, the bank's payment is invalid against the trustee. I must conclude that the Court has reasoned that a contractual defense retained against the bankrupt suffices to preclude use of a power expressly conferred upon the trustee. If this is the Court's meaning, it has traversed both logic and authority, and has emasculated the powers given to trustees under the Act.

The Court's principal contention seems to be that equitable considerations oblige it to release the bank from liability. Its premise plainly is that equity is here a solvent to which we may appropriately resort; I am unable to accept that premise. This is not a case in which the statute is imprecise. Nor is it a case in which the legislature's intentions have been misshapen by the statute's words; even a cursory examination of the history of § 70 will evidence that its terms faithfully reflect Congress' purposes.

The Act of 1898 vested title to the bankrupt's property in the trustee at adjudication, but contained noth-

ing to prevent its dissipation in the interval after filing.[3] The courts were therefore left free to devise protective rules to reconcile the competing interests of the estate and of those who dealt with the bankrupt in this period. The fulcrum of those rules was the proposition that a "petition in bankruptcy is a caveat to all the world, and in effect an attachment and injunction." *Mueller* v. *Nugent*, 184 U. S. 1, 14. The courts softened its severity by a series of exceptions, either employing or distinguishing it as equity or convenience suggested. The result, as a principal draftsman of the Chandler Act reforms described it, was that "no consistent theory of protected transactions developed," and the situation was "conducive to confusion and uncertainty, with potentialities for argument, 'bluffing,' litigation, expense and delay."[4] The law consisted essentially of "nebulous vagaries."[5]

The Chandler Act stemmed chiefly from a sustained investigation of these and other problems by the National Bankruptcy Conference.[6] Its members were the Act's principal draftsmen. The revisions they made to § 70 entirely restructured the basis both of the trustee's title and of the protection given to transactions which occur after filing. Their purpose, as one of them explained to the Chandler subcommittee, was to provide "a clear statutory basis" to the issues of title and protected transactions, in "lieu of a crazy quilt of contra-

[3] This Court had held that despite the cleavage at adjudication, the trustee took the title as it was at filing. *Everett* v. *Judson*, 228 U. S. 474. The situation is summarized in McLaughlin, Aspects of the Chandler Bill to Amend the Bankruptcy Act, 4 U. Chi. L. Rev. 368, 383.

[4] McLaughlin, Amendment of the Bankruptcy Act, 40 Harv. L. Rev. 341, 615. The same conclusions are reached by Weinstein, The Bankruptcy Act of 1938, at 161.

[5] 4 Collier, Bankruptcy ¶ 70.66, at 1495.

[6] A brief history of the Conference's work may be found in McLaughlin, 4 U. Chi. L. Rev., at 375.

dictory judicial statements."[7] The effect of their revisions was to define "the full extent to which bona fide transactions with the bankrupt, after bankruptcy, will be protected."[8]

Adjudication and receivership were plainly expected to mark the perimeters of this protection. Various factors determined this choice. First, none of the several exceptions to *Mueller* v. *Nugent* reached transactions which occurred after adjudication.[9] More important, once the draftsmen had elected to vest title in the trustee from filing, they were chiefly anxious to shield debtors from the consequences of unwarranted involuntary petitions.[10] They feared that such a petition might ruin a debtor by inducing others to avoid dealings with him.

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[7] Hearings before the House Committee on the Judiciary on H. R. 6439, 75th Cong., 1st Sess., 212. Professor McLaughlin quoted from his article in 40 Harv. L. Rev. 341. He subsequently acknowledged that § 70 would permit an area in which the courts could continue to balance the competing interests of the parties. *Ibid.* In light of the importance attached to adjudication as a line of cleavage, and the comparative insignificance intended for § 70 (d) in voluntary proceedings, see *infra*, I do not believe that this acknowledgment can be taken to reach this case.

[8] 4 Collier, Bankruptcy ¶ 70.67, at 1500.

[9] 4 Collier, Bankruptcy ¶ 70.66, at 1498. In the one apparent exception, *Jones* v. *Springer*, 226 U. S. 148, a dredge had been placed in the hands of a receiver under an attachment levied before filing. The Court concluded that this sufficed to avoid the ordinary limitations imposed by adjudication.

[10] Hearings before the House Committee on the Judiciary on H. R. 6439, 75th Cong., 1st Sess., 211. Professor McLaughlin described this to the subcommittee as "the next most pressing problem." He concluded that "we have put in a provision [70 (d)] to cover that [the problem of unwarranted petitions]." His explanation to the subcommittee of § 70 (d) was based entirely on this problem. There is of course evidence that the draftsmen also expected to alleviate unfairness which § 70 (a) might otherwise produce. See Analysis of H. R. 12889, House Committee on the Judiciary, 74th Cong., 2d Sess., 230.

Section 70 (d) was expected to immunize bona fide transactions after filing, and thus to encourage dealings with the solvent debtor. There is no need for such protection after adjudication. Finally, adjudication and receivership signal the beginning of bankruptcy administration, and they are therefore both appropriate moments at which to forbid all further meddling with the estate.[11]

It is equally plain that the protection offered by § 70 (d) must have been intended principally for involuntary proceedings. There are several indications of this. Most important, the hazard to which the section was chiefly directed, the consequences of an unwarranted petition upon a debtor's credit, is entirely absent from voluntary proceedings. Thus, the discussion of this problem before the Chandler subcommittee was explicitly confined to involuntary petitions.[12] Further, the protection offered by § 63 (b), which closely supplements § 70 (d), extends only to involuntary proceedings.[13] Finally, the draftsmen must surely have known that the adjudication of voluntary petitions ordinarily followed quickly and routinely after filing.[14] It was certainly not unknown for adjudication to occur on the day of filing.[15] The draftsmen could only have intended

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[11] MacLachlan, Handbook of the Law of Bankruptcy, 346.

[12] Hearings before the House Committee on the Judiciary on H. R. 6439, 75th Cong., 1st Sess., 211,

[13] 52 Stat. 873, 11 U. S. C. § 103 (b). Section 63 (b) provides that "In the interval after the filing of an involuntary petition and before the appointment of a receiver or the adjudication, whichever first occurs, a claim arising in favor of a creditor by reason of property transferred or services rendered by the creditor to the bankrupt for the benefit of the estate shall be provable to the extent of the value of such property or services."

[14] MacLachlan, Handbook of the Law of Bankruptcy, 40.

[15] See, *e. g.*, *New York County National Bank* v. *Massey*, 192 U. S. 138.

that any protection given in voluntary proceedings by § 70 (d) be fleeting and minimal.[16]

In short, § 70 was tailored to provide carefully measured protection to bona fide transfers. It was intended to preclude further confusion and uncertainty. There is every indication that its terms faithfully reflect its purposes.

I fully sympathize with the discomfort of the bank's position, but I cannot escape the impact of what Congress has done.[17] The Court has not found § 70 constitutionally impermissible.[18] It has simply measured

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[16] Further, the 1959 amendments to § 18, by which adjudication results by operation of law from filing, were adopted upon the recommendation of the Judicial Conference and its Committee on Bankruptcy Administration. Annual Report of the Proceedings of the Judicial Conference, 1958, p. 28. The bill received the endorsement of the National Bankruptcy Conference. H. R. Rep. No. 241, 86th Cong., 1st Sess., 2. It therefore seems quite improbable that the 1959 amendments could have inadvertently excluded voluntary proceedings from the scope of § 70 (d).

[17] Judge Soper's reasoning in *Lake* v. *New York Life Insurance Co.*, 218 F. 2d 394, 399, seems entirely persuasive: "Whether the line which has been drawn is the best possible solution is not for the courts to say. The line has in fact been drawn by competent authority and it is no longer necessary for the courts to make the attempt, which has not been conspicuously successful in the past, to decide cases on the facts as they arise. . . ." See also *Kohn* v. *Myers*, 266 F. 2d 353.

[18] I cannot in any event accept petitioner's contention that these provisions have denied it due process. In exercise of its express constitutional authority over bankruptcy, Art. I, § 8, Congress has attached great importance to swift and efficient administration; to this purpose it devised a statutory scheme by which it balanced the competing rights of the interested parties. Congress' purposes are permissible, and the scheme it has adopted is reasonably calculated to achieve those purposes. In this context I cannot say that the Constitution requires that all whose rights may be reached by bankruptcy proceedings must first have actual notice of them. Cf. *Hanover National Bank* v. *Moyses*, 186 U. S. 181.

the statute by the standard of its own conscience, and concluded that equity requires a result which the statute forbids. I had thought it well settled that equity may supplement, but may never supersede the Act. 1 Collier, Bankruptcy ¶ 2.09, at 171–172. The Act's language is neither imprecise nor infelicitous; I can therefore see no room for the interposition of equity.

More important, the Court today permits the dilution of the Chandler amendments to § 70. The Court's disposition of this case may be taken to suggest that whenever equity is thought strongly to demand relief from the strictures of the Act, further exceptions may be appropriately created to the statutory scheme. I fear that the Court may have set in motion once more the protracted process which before 1938 resulted in "confusion and uncertainty," "litigation, expense and delay." If so, the Chandler amendments will have had no more permanent result than to wipe the judicial slate momentarily clean.

I would affirm the judgment of the Court of Appeals.

SUPREME COURT OF THE UNITED STATES

No. 63.—October Term, 1966.

Bank of Marin, Petitioner, v. John M. England, Trustee in Bankruptcy.	On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit.

[November 21, 1966.]

Mr. Justice Fortas.

I would vacate the judgment. I believe that we do not have before us a case or controversy between the parties of record.

Respondent, the trustee in bankruptcy, has no substantial stake in the outcome of this litigation and is not an adversary in the usual sense. On February 24, 1964, the referee in bankruptcy ruled that both the petitioner bank and the payee on the bankrupt's checks were liable to the trustee. On May 19, 1964, the payee paid the trustee in full and has not been a party to this litigation since that time. Having received full payment, the trustee has no interest in the litigation except professional curiosity as to the question of law—and he so apprised the District Court, the Court of Appeals, and this Court. See Brief for Respondent, p. 2. See also Petition for Certiorari, p. 4. Nevertheless, the bank, also eager for an answer to this intriguing legal problem and facing a claim from the payee for contribution, continued the litigation against the trustee, and the trustee obligingly went along. The respondent trustee's only financial interest is admittedly confined to the question of court costs,[1] incurred as a volunteer.

[1] An unbroken line of cases establishes the rule that controversy as to costs alone does not salvage an otherwise moot case. See, *e. g.*, *Walling* v. *Reuter Co.*, 321 U. S. 671, 677 (1944); *United*

There are two reasons of substance why the Court should not, in this case, decide the important statutory question presented. First, this is not an adversary proceeding, and has not been one since respondent received full payment in 1964. It is basic to our adversary system to insist that the courts have the benefit of the contentions of opposing parties who have a material, and not merely an abstract, interest in the conflict. Adverse parties—adverse in reality and not merely in positions taken—are absolutely necessary. See, *e. g.*, *Muskrat* v. *United States*, 219 U. S. 346, 361–363 (1911); *California* v. *San Pablo & Tulare R. R.*, 149 U. S. 308, 313–314 (1893); *South Spring Gold Co.* v. *Amador Gold Co.*, 145 U. S. 300, 301–302 (1892). Cf. *Aetna Life Ins. Co.* v. *Haworth*, 300 U. S. 227, 240–242 (1937) (Hughes, C. J.); *Fairchild* v. *Hughes*, 258 U. S. 126, 129–130 (1922) (Brandeis, J.).

Second, this is a peculiar case in which to depart from the settled rule. The effect of the decision today is to strip the payee of its asserted right to contribution, although the payee is not before this Court, and was not before the Court of Appeals or the District Court. The question of the relative rights and obligations of the payee and the bank ought to be resolved in litigation in which both participate.[2] Cf. *Mullane* v. *Central Hanover Tr. Co.*, 339 U. S. 306, 314 (1950). The impact of

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States v. *Anchor Coal Co.*, 279 U. S. 812 (1929); *Alejandrino* v. *Quezon*, 271 U. S. 528, 533–536 (1926); *Brownlow* v. *Schwartz*, 261 U. S. 216 (1953); *Heitmuller* v. *Stokes*, 256 U. S. 359, 362–363 (1921); Robertson & Kirkham, Jurisdiction of the Supreme Court of the United States § 274 (Wolfson & Kurland ed.); 6 Moore, Federal Practice ¶ 54.70 (5), at 1311 (2d ed. 1966).

[2] Upon vacation of the judgment below, the bank would be free to relitigate with the payee the question of its own liability, since the bank was in no respect responsible for the manner in which this case became a nonadverse proceeding. See *United States* v. *Munsingwear*, 340 U. S. 36, 39–40 and n. 1 (1950).

today's decision upon a party not present confirms the wisdom of the rule "that when there is no actual controversy, involving real and substantial rights, between the parties to the record, the case will be dismissed." *Little* v. *Bowers*, 134 U. S. 547, 557. See also *Lord* v. *Veazie*, 8 How. 251, 255.

I would vacate the judgment below and remand with direction to dismiss. See *Mechling Barge Lines* v. *United States*, 368 U. S. 324, 329–330 (1961); *United States* v. *Munsingwear*, 340 U. S. 36, 39–41 (1950).